IN THE

SUPREME COURT OF THE UNITED STATES

October Term 1937

No. 641.

J. D. ADAMS MANUFACTURING COMPANY,
Appellant,

v.

WILLIAM STOREN, as Chief Administrative Officer of the Department of Treasury of the State of Indiana,

DEPARTMENT OF TREASURY OF THE STATE OF INDIANA,

PAUL V. McNUTT, WILLIAM STOREN, FLOYD E. WILLIAMSON, as and Constituting the Board of Department of Treasury of the State of Indiana,

PHILIP LUTZ, JR., as Attorney General of the State of Indiana,

Appellees.

Appeal From the Supreme Court of the State of Indiana.

APPELLEES' BRIEF.

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Attorney General of Indiana,
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Note:—All italics used in quotations in this brief are ours unless otherwise stated.

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THE OPINION BELOW.

The opinion below, rendered by the Supreme Court of Indiana on April 30, 1935, is not yet officially reported. It is contained in this record at pages 43 to 60, and is reported in 7 Northeastern Reporter (Second Series), 941.

STATEMENT OF THE CASE.

This is an appeal from the judgment of the Supreme Court of the State of Indiana (R. 42 and 43) in an action originally instituted in the Marion Superior Court by the J. D. Adams Manufacturing Company, an Indiana corporation (the appellant here), seeking a declaratory judgment construing certain portions (more particularly, sections 1 (f) and 6 (a)) of Chapter 50 of the Acts of the General Assembly of Indiana of 1933 (p. 388 at pp. 389-390-392-393; 11 Burns' Indiana Statutes, 1933 Ed., secs. 64-2601 to 64-2629; Baldwin's Indiana Statutes, 1934 Ed., secs. 15,981 to 16,010).

The appeal involves two distinct questions:

The first question involved in this appeal is: Can the provisions of Chapter 50 of the Indiana Acts of 1933 (which imposes a general non-discriminatory excise upon all who are domiciled within the State of Indiana or who transact business within the state and under its protection measured by the amount of gross income) be applied to all of the gross income of the appellant (an Indiana corporation), including that portion which is received in Indiana from the sale of products manufactured in Indiana shipped from appellant's factory in Indiana to purchasers in other states and foreign countries; or is such an application of the Act prohibited by the provisions of Clause 3 of Section 8 or Section 10 of Article I of the Constitution of the United States? (R. 70.)

The second of these is: Can the provisions of Chapter 50 of the Indiana Acts of 1933 be construed to apply to that part of appellant's gross income which accrues as interest payments on municipal corporation bonds, which

were exempt from property taxation by statute, without impinging upon the prohibition of section 10 of Article I of the Federal Constitution that "no state shall * * * pass any * * * law impairing the obligation of contracts"? (R. 70-71.)

The statutes appertaining to the *first* question presented by this appeal are as follows:

Chapter 50 of the Indiana Acts of 1933, in so far as it applies to this feature of this appeal, provides as follows:

> "The term 'gross income,' except as hereinafter otherwise expressly provided, means the gross receipts of the taxpayer received as compensation for personal services, and the gross receipts of the taxpayer derived from trades, businesses or commerce, and the gross receipts proceeding or accruing from the sale of property, tangible or intangible, real or personal, or service, or any or all of the foregoing, and all receipts by reason of the investment of capital, including interest, discount, rentals, royalties, fees, commissions or other emoluments, however designated, and without any deductions on account of the costs of property sold, the cost of materials used, labor cost, interest or discount paid, or any other expense whatsoever, and without any deductions on account of losses; Provided, however, That the term 'gross income' shall not include cash discounts allowed and taken on sales; nor freight prepaid by the taxpayer and repaid to him by the purchaser; goods, wares or merchandise, or the value thereof, returned by customers when the sale price is refunded either in cash or by credit; nor the sale price of any article accepted as part payment on any new article sold, if and when the full sale price of the new article is included in the 'gross income' subject to taxation under this act; Provided, further, That 'gross income' shall include

the proceeds from the sale of any property handled on consignment by the taxpayer."

Sec. 1 (f), Chapter 50, Indiana Acts of 1933, p. 388, at pp. 389-390;

11 Burns' Indiana Statutes, 1933 Ed., 64-2601 (f);

Baldwin's Indiana Statutes, 1934 Ed., 15,981 (f).

"There is hereby imposed a tax, measured by the amount or volume of gross income, and in the amount to be determined by the application of rates on such gross income as hereinafter provided. Such tax shall be levied upon the entire gross income of all residents of the State of Indiana, and upon the gross income derived from sources within the State of Indiana, of all persons and/or companies, including banks, who are not residents of the State of Indiana, but are engaged in business in this state, or who derive gross income from sources within this state, and shall be in addition to all other taxes now or hereafter imposed with respect to particular occupations and/or activities. Said tax shall apply to, and shall be levied and collected upon, all gross incomes received on or after the first day of May, 1933, with such exceptions and limitations as may be hereinafter provided."

Sec. 2, Chapter 50, Indiana Acts of 1933, p. 388 at p. 390;

11 Burns' Indiana Statutes, 1933 Ed., 64-2602;

Baldwin's Indiana Statutes, 1934 Ed., 15,982.

"The tax hereby provided for shall be imposed at the following rates:

(a) Upon the entire gross income of every person engaged in the business of manufacturing, compounding, or preparing for sale, profit, or use, any article or articles, substance or substances, commodity or commodities; or in the business of mining and/or producing for sale, profit or commercial use any oil, natural gas, stone, coal, sand, gravel or other mineral product, or felling and producing timber, for sale, profit or commercial use; or in agriculture, including the production of live stock, poultry, eggs, or any other product of the farm, orchard, garden or greenhouse, one-fourth of one per cent."

* * * * * * *

(c) Upon the entire gross income of every person engaged in the business of retailing of any tangible commodity or commodities not specifically mentioned in subsection (d) of this section, one per cent."

* * * * * * *

Sec. 3 (a), (c), Chapter 50, Indiana Acts of 1933, p. 388 at p. 391;
11 Burns' Indiana Statutes, 1933 Ed., 64-2603 (a), (c);
Baldwin's Indiana Statutes, 1934 Ed., 15,983 (a), (c).

"There shall be excepted from the gross income taxable under this act:

'So much of such gross income as is derived from business conducted in commerce between this state and other states of the United States, or between this state and foreign countries, to the extent to which the State of Indiana is prohibited from taxing under the Constitution of the United States of America. There shall also be excepted from such

gross income, salaries, pensions, and other emoluments paid by the United States of America or any of its agencies, and interest or other earnings paid upon bonds or other securities issued by the United States of America or its agencies, to the extent that the State of Indiana is prohibited from imposing a tax upon such salaries, pensions, emoluments, interest and/or earnings, by the Constitution of the United States of America.' "

Sec. 6 (a), Chapter 50, Indiana Acts of 1933, pp. 392-393;

11 Burns' Indiana Statutes, 1933 Ed., 64-2606 (a);

Baldwin's Indiana Statutes, 1934 Ed., 15,986 (a).

The appellant is a corporation organized under the laws of the State of Indiana (R. 24), engaged in manufacturing machinery, tools, appliances, and equipment for the construction, improvement, and repair of roads and highways (R. 25). Its home office (R. 24), principal place of business (R. 24), and its only manufacturing plant (R. 24, 25) are located within the State of Indiana. Appellant sells a substantial portion of its products to purchasers within the State of Indiana (R. 28), and a substantial portion of its products, through selling agents and otherwise, to dealers in other states and foreign countries (R. 25, 26, 27). All sales made to purchasers located outside of the State of Indiana are upon orders taken subject to the approval of the home office (R. 26, 27), shipment is made from the factory (R. 26, 27, 28), and payment is made to the home office located in Indiana (R. 26, 27).

The facts have been stipulated (R. 24 to 35), and there is now no disagreement as to the amount of the tax, if any, but merely as to the validity of the application of the

Act to the specific income in question in view of the provisions of Article I, Section 8 and 10, of the Federal Constitution.

The statutes appertaining to the *second* question presented by this appeal, relating to the inclusion of interest derived from bonds exempt from property taxation in the index for the excise tax presently before the court, are:

Section 5 of Chapter 59 of the Indiana Acts of 1919 (p. 198 at pp. 199, 203); 11 Burns' Indiana Statutes, 1933 Ed., 64-201, cl. 20; Baldwin's Indiana Statutes, 1934 Ed., 15,518, cl. 20) provides:

> "Sec. 5. The following property shall be exempt from taxation:"
>
> (Then follow nineteen clauses listing specific exemptions.)
>
> "Twentieth. All bonds, notes, and other evidence of indebtedness hereafter issued by the State of Indiana or by municipal corporations within the state upon which the said state or the said municipal corporations pay interest, shall be exempt from taxation."

In the same act, section 25 of Chapter 59 of the Indiana Acts of 1919 (p. 198 at p. 210); 11 Burns' Indiana Statutes, 1933 Ed., 64-506; Baldwin's Indiana Statutes, 1934 Ed., 15,518), provides:

> "Section 25. Where bonds or stocks are now or may hereafter be exempted from taxation, the accrued interest on such bonds or dividends on such stocks shall be listed and assessed, unless otherwise exempted, without regard to the time when the same is to be paid."

Chapter 50 of the Indiana Acts of 1933, an Act of general application upon all domiciled in (or non-residents

conducting business within) Indiana, insofar as it applies to this feature of the appeal, provides as follows:

> "The term 'gross income,' except as hereinafter otherwise expressly provided, means the gross receipts of the taxpayer received as compensation for personal services, and the gross receipts of the taxpayer derived from trades, businesses or commerce, and the gross receipts proceeding or accruing from the sale of property, tangible or intangible, real or personal, or service, or any or all of the foregoing, and all receipts by reason of the investment of capital, including interest, discount, rentals, royalties, fees, commissions or other emoluments, however designated, and without any deductions on account of the costs of property sold, the cost of materials used, labor cost, interest or discount paid, or any other expense whatsoever, and without any deductions on account of losses; Provided, however, That the term 'gross income' shall not include cash discounts allowed and taken on sales, nor freight prepaid by the taxpayer and repaid to him by the purchaser; goods, wares or merchandise, or the value thereof, returned by customers when the sale price is refunded either in cash or by credit; nor the sale price of any article accepted as part payment on any new article sold, if and when the full sale price of the new article is included in the 'gross income' subject to taxation under this act; Provided, further, That 'gross income' shall include the proceeds from the sale of any property handled on consignment by the taxpayer."

Sec. 1 (f), Chapter 50, Indiana Acts of 1933, p. 388 at pp. 389-390;

11 Burns' Indiana Statutes, 1933 Ed., 64-2601 (f);

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"There is hereby imposed a tax, measured by the amount or volume of gross income, and in the amount to be determined by the application of rates on such gross income as hereinafter provided. Such tax shall be levied upon the entire gross income of all residents of the State of Indiana, and upon the gross income derived from sources within the State of Indiana, of all persons and/or companies, including banks, who are not residents of the State of Indiana, but are engaged in business in this state, or who derive gross income from sources within this state, and shall be in addition to all other taxes now or hereafter imposed with respect to particular occupations and/or activities. Said tax shall apply to, and shall be levied and collected upon, all gross incomes received on or after the first day of May, 1933, with such exemptions and limitations as may be hereinafter provided."

Section 2, Chapter 50, Indiana Acts of 1933, p. 388 at p. 390;

11 Burns' Indiana Statutes, 1933 Ed., 64-2602;

Baldwin's Indiana Statutes, 1934 Ed., 15,982.

The facts having been mutually stipulated by the parties, there is now no disagreement as to the facts, the amount of the tax, if any, but merely as to the validity of the application of the Act to the income in question (R. 24 to 35, more particularly, R. 29).

The right of the State of Indiana to collect approximately $11,000,000.00 in taxes is involved in this appeal.

SUMMARY OF ARGUMENT.

PROPOSITION I.

The Tax Imposed by the Indiana Act is a Tax Upon the Receipt of Gross Income, a Privilege Tax, and Does Not Burden Interstate Commerce in the Constitutional Sense.

> "That the receipt of income by a resident of the territory of a taxing sovereignty is a taxable event is universally recognized."

State of New York ex rel. Cohn v. Graves, et al., (1937) 300 U. S. 308, 81 L. Ed. 666;
Maguire v. Trefry, (1920), 253 U. S. 12;
Lawrence v. State Board of Tax Commissioners, (1932), 286 U. S. 276.

The Supreme Court of the State of Indiana has held not only in the case at bar, but in other cases wherein the tax in question was involved, that such a tax was imposed upon the receipt of gross income, a privilege tax.

Miles, et al. v. Department of Treasury, (1935), 209 Ind. 172, 199 N. E. 372, 101 A. L. R. 1359;
Indiana Creosoting Co. v. McNutt, etc., et al., (1936), — Ind. —, 5 N. E. (2d) 310, 313;
See also: Sec. 2, Chap. 50, Indiana Acts of 1933, p. 388 at p. 390; 11 Burns' Ind. Statutes, 1933 Ed., 64-2602; Baldwin's Indiana Statutes, 1934 Ed., 15,982;
Storen v. J. D. Adams Manufacturing Co., (1937), 7 N. E. (2d) 941.

It was the purpose of the tax in question to relieve and lessen the burden of taxes in the state on tangible

property. The Supreme Court of Indiana in discussing this question says:

> "The statute was enacted concurrently with other legislation limiting levies upon property. The greater portion of the revenue raised goes back to local units of government for the maintenance of schools and other activities otherwise dependent upon property levies. Legislative history indicates that one of the purposes of the Gross Income Tax Law was to redistribute governmental burdens and relieve property of a tax burden which was thought to be too great."
>
> *Storen v. J. D. Adams Manufacturing Co.,* (1937), 7 N. E. Rep. (2nd) 941 at p. 944;
> See Limitation of Tax Levies Act; Acts of Indiana 1933, page 1085.

The law was intended to be and is general in its application and operates upon all residents of the state who receive income within its borders. This is not a tax levied on selected or special groups or enterprises. It is a general tax levied upon all persons, firms or corporations resident and/or domiciled within the State of Indiana and imposed upon the privilege of receiving income within the State, and measured by the amount of volume thereof. It was designed to lessen the burden of tax on real estate and tangible property, and to spread the tax base, to the end that all persons receiving income in the State of Indiana might be made to bear a fair portion of the costs of government, and thereby make some return to the state for the privileges afforded by the state that are incident to domicile.

The tax does not violate the Constitution of the United States by laying an illegal burden on interstate commerce and does not levy an impost or duty upon exports under either Section 8 or Section 10, of Article I of the Federal

Constitution. This is true for each of the following reasons:

First: The tax is general in its application and was adopted as a means of distributing the burden of the cost of government commonly levied on tangible property.

> *U. S. Glue Co. v. Oak Creek,* 247 U. S. 321, 329;
> *Peck & Co. v. Lowe,* 247 U. S. 165;
> *Virginia v. Imperial Coal Co.,* 293 U. S. 15;
> *Postal Telegraph Cable Co. v. Adams,* 155 U. S. 688, 696;
> *Adams Express Co. v. Ohio,* 165 U. S. 194, 220;
> *Atlantic & Pacific Telegraph Co. v. Philadelphia,* 190 U. S. 160, 163;
> *United States Express Co. v. Minnesota,* 223 U. S. 335, 344;
> *Cudahy Packing Co. v. Minnesota,* 246 U. S. 450, 453;
> *Eastern Air Transport v. Tax Commission,* 285 U. S. 147, 152.

Second: The tax imposes no direct burden on interstate commerce. It is not laid on income from exportation because of its source or in a discriminative way, but just as it is laid on other income. It is both nominally and actually a general tax. Interstate commerce is affected only incidently and indirectly in the same manner which results from the payment of property taxes or any other general contribution which a citizen makes to the cost of government.

> *Cudahy Packing Co. v. Minnesota, supra;*
> *St. Louis Southwestern Ry. Co. v. Arkansas,* 235 U. S. 350, 367;

United States Express Co. v. Minnesota, supra;
Galveston, Harrisburg & San Antonio Ry. Co. v. Texas, 210 U. S. 217;
Pullman Co. v. Richardson, 261 U. S. 330, 339;
Peck & Co. v. Lowe, 247 U. S. 165.

Third: The Act in question does not discriminate against interstate commerce. It is not a tax levied on selected enterprises engaged wholly or largely in interstate transactions, nor is there any contention that the tax imposed is not in proportion to the privilege enjoyed. The tax is general in its application and non-discriminatory in its burden. Its operation and effect is to impose a legitimate burden upon the privilege of receiving gross income within the State of Indiana and the rights attendant thereon incident to domicile within the state. It produces no direct burden on commerce and only the same kind of incidental and indirect effect is experienced as that which results from the payment of property taxes or any other general contribution to the cost of government. It, therefore, does not amount to a regulation of interstate commerce.

American Manufacturing Co. v. City of St. Louis, (1919), 250 U. S. 459, 39 Sup. Ct. 522;
Hope Natural Gas Co. v. Hall, (1927), 274 U. S. 284, 288;
Flint v. Stone Tracy Co., (1911), 220 U. S. 107;
Home Insurance Co. v. New York, (1890), 134 U. S. 594;
U. S. Express Co. v. Minnesota, (1912), 223 U. S. 335, 32 Sup. Ct. 211;
Kansas City, F. S. and N. P. Co. v. Botkin, (1916), 240 U. S. 227, 60 L. Ed. 617, 36 Sup. Ct. 261;

Hump Hairpin Manufacturing Co. v. Emmerson, (1922), 258 U. S. 290, 66 L. Ed. 622, 42 Sup. Ct. 305;

Northwestern Mutual Life Insurance Co. v. Wisconsin, (1918), 247 U. S. 132, 38 Sup. Ct. 414.

This tax law has been in operation in the State of Indiana since May, 1933. It was intended to reduce and has operated to reduce the tax burden on real estate and personal property. Approximately fourteen million dollars per year of the revenues produced from this source are returned to the school corporations of the state for the payment, in part, of teachers' salaries. The whole tax program of the State of Indiana has been influenced by the act in question. It is the duty of this Court, therefore, in passing upon the validity of this tax law, to view generally the scheme of taxation as it now exists in the State of Indiana to determine whether or not the program, as operative, imposes an undue burden upon interstate commerce.

This Court has said:

> "* * * we are to look for a practical rather than a logical or philosophical distinction"

in approaching the problems of the jurisdiction to tax as affected by the commerce clause.

Galveston, H. and S. A. Ry. v. Texas, (1908), 210 U. S. 217, 225, 227; 28 Sup. Ct. 638, 640.

Disregarding doctrinal disquisitions then, and regarding the results of the decisions, the constant controlling motive of this Court has been the proper desire to prevent states from imposing on interstate commerce any unusual or peculiar burden. Property having its situs within the taxing state is not exempted from a non-discriminatory

tax upon the property merely because such property is used in interstate commerce.

> *Pullman Palace Car Co. v. Pennsylvania,* (1891), 141 U. S. 18;
>
> *Western Union Tel. Co. v. Taggart,* (1896), 163 U. S. 1.

From these decisions—and those dealing with a *general* net income tax (*United States Glue Co. v. Oak Creek,* (1918), 247 U. S. 321, 329, 38 Sup. Ct. 499, 501); those dealing with gross receipts taxes as substitutes, in whole or in part, for taxes on property (*Maine v. Grand Trunk Ry.,* (1891), 142 U. S. 127, 12 Sup. Ct. 121; *Cudahy Packing Co. v. Minnesota,* (1918) 246 U. S. 450, 38 Sup. Ct. 373; *United States Express Co. v. Minnesota,* (1912), 223 U. S. 235, 32 Sup. Ct. 328; *Northwestern Life Insurance Co. v. Wisconsin,* (1918), 247 U. S. 132, 38 Sup. Ct. 444; *Pullman Co. v. Richardson,* (1923), 261 U. S. 330, 43 Sup. Ct. 366); those dealing with privilege taxes (*American Manufacturing Co. v. City of St. Louis,* (1919), 250 U. S. 459, 39 S. Ct. 522, 63 L. Ed. 1084; *Oliver Mining Co. v. Lord,* (1923), 262 U. S. 172, 43 Sup. Ct. 526),—it is important to recognize that the propositions announced and the results reached are based upon the premise that individuals, firms and corporations are not absolved from the payment of their proper proportion of the cost of government in the state of domicile, or the cost of government in the state in which the property is situated, merely because the person domiciled, or the owner of the property, is engaged in interstate commerce. Every individual, firm or corporation domiciled or doing business within a state is bound, upon the simplest statement of common justice, to bear its proportion of governmental expense.

Statements made by the court and relied upon by the appellant, to the effect that a tax on gross receipts is a direct burden on interstate commerce, have never been applied to a general tax. Such statements have appeared in support of a net income tax or taxes imposed upon a special group. But, even as applied to net income, economists all agree that there exists a very definite relationship between gross receipts and net profits.

See dissenting opinion *Stewart Dry Goods Co. v. Lewis,* 294 U. S. 566.

The State of Indiana has a right to impose a tax on the privilege of receiving income as an incident to the right of domicile. The tax so imposed, measured by the amount of gross receipts, is more general in its application than any other tax now imposed. It has lessened the burden of tax on tangible property—it has imposed no direct burden on interstate commerce,—it has not discriminated against those engaged therein.

Its validity should therefore be sustained.

PROPOSITION II.

No Contract Exempting Interest Having Been Entered Into, This Tax Is Not Invalid as Impairing the Obligation of a Contract.

Statutory exemptions of property from taxation, such as the one in the instant case, are not contractual, and therefore not within the purview of section 10 of Article I of the Federal Constitution, for the reasons that: (a) in order that a state may be bound by a statutory exemption there must be a binding contract supported by considera-

tion; (b) a mere gratuity or bounty does not amount to a contract; (c) a general statutory exemption from taxation is construed to be a gratuity, and not a contract. In the instant case there was no consideration for the exemption from property taxation of the bonds held by the appellant, and hence there was no contract.

> *East Saginaw Salt Mfg. Co. v. City of East Saginaw*, (187 , 13 Wall. 373, 20 L. Ed. 611;
> *Wisconsin and Michigan Railway Co. v. Powers*, (1903), 191 U. S. 379, 48 L. Ed. 299;
> *Grand Lodge of the State of Louisiana v. City of New Orleans*, (1897), 166 U. S. 143, 41 L. Ed. 951;
> *Shiner v. Jacobs*, ( ), 62 Iowa 392, 17 N. W. 613;
> *Miller v. Hagemann*, ( ), 114 Iowa 195, 86 N. W. 281.

An exemption from taxation is never to be implied or presumed. Such an intention must be affirmatively expressed in clear and unmistakable terms.

> *Great Northern Railroad Co. v. Minnesota*, (1910), 216 U. S. 206, 221, 54 L. Ed. 446, 30 S. Ct. 344;
> *Henderson Bridge Co. v. City of Henderson*, (1899), 173 U. S. 592, 617, 618, 43 L. Ed. 823, 19 S. Ct. 553;
> *Millsaps College v. Jackson*, (1927), 275 U. S. 129, 132;
> *Hale v. Iowa State Board of Assessment and Review*, (Nov., 1937), 82 L. Ed. Advance Opinions, 66 at 70;
> *Pacific Co. v. Johnson*, (1932), 285 U. S. 480, 491, 76 L. Ed. 893, 897, 52 S. Ct. 434;

Methodist Episcopal Church v. Ellis, (1871), 38 Ind. 3, 8;

Storen, etc., et al. v. Jasper County Farm Bureau Cooperative Association, (1936), 102 Ind. App. —, 2 N. E. (2d) 432 at 434;

2 Cooley on Taxation, (4th Ed.) sec. 672, pp. 1403, 1404, 1405.

Moreover, if an exemption is found to exist, it must not be enlarged by construction, since the presumption is that the legislative body has granted in express terms all it intended to grant.

2 Cooley on Taxation, (4th Ed.), sec. 672, pp. 1408, 1409, 1410, 1411;

Ford v. Delta and Pine Land Co., (1897), 164 U. S. 662, 666, 41 L. Ed. 590, 17 Sup. Ct. 230;

Central Railroad and Banking Co. v. Wright, (1896), 164 U. S. 327, 335, 336, 41 L. Ed. 454, 17 Sup. Ct. 80.

The Indiana statute under which the exemption is claimed by the appellant applies exclusively to *general property taxes* by *its very terms,* and not to an excise tax.

Sec. 5, Chapter 59, Indiana Acts of 1919, p. 198 at 199, 203; 11 Burns' Indiana Statutes, 1933 Ed., 64-201; Baldwin's Indiana Statutes, 1934 Ed., 15,518;

See: *Hale v. Iowa State Board of Assessment and Review,* (Nov. 1937), 82 L. Ed. Advance Opinions, 66.

The statute under which appellant claims an exemption from excise taxation of the interest derived from the

ownership of bonds exempted from general property taxes contains internal positive evidence that the legislative body in granting the exemption to the bonds from the general property taxes, did not intend that the interest derived from such bonds or other evidences of indebtedness, should be accorded the same bounty.

> Section 25, Chapter 59, Acts of Indiana of 1919, p. 198 at p. 210; 11 Burns' Indiana Statutes, 1933 Ed., 64-506; Baldwin's Indiana Statutes, 1934 Ed.

A general tax upon the fruits of domicile, the receipts, custody and control of income, measured by the receipt of gross income, such as that contained in Chapter 50 of the Indiana Acts of 1933, pp. 388 to 407, is not a tax upon property but an excise tax, and the Indiana Supreme Court has so held.

> *Miles et al. v. Department of Treasury et al.*, (1935), 209 Ind. 172; 199 N. E. 372, 101 A. L. R. 1359.

People, etc., ex rel. Clyde v. Gilchrist, (1923), 262 U. S. 94, 64 L. Ed. 883, is authority for the proposition that the general tax on the fruits of domicile, i. e., the receipt, custody and control of income, imposed by the Indiana Act, measured by the receipt of gross income, does not violate the protection granted by the contract clause of section 10 of article 1 of the Federal Constitution.

The cases upon which the appellant relies, as holding that to tax the interest is to tax the bonds, are not authoritative with reference to the question presented in this appeal.

(a). Several are decisions which discuss the power

of a state to tax the federal government or its instrumentalities.

> *Northwestern Mutual Life Insurance Co. v. Wisconsin,* (1927), 275 U. S. 136;
>
> *Gillespie v. Oklahoma,* (1922), 257 U. S. 501, 66 L. Ed. 338;
>
> *Weston v. Charleston,* (1829), 27 U. S. 449.

(b). The decison of *Macallen Co. v. Massachusetts,* (1929), 279 U. S. 620, is not applicable, for the following reasons: first, the exemption statute there involved specifically exempted *persons* as well as property; second, in that instance the taxing statute, by amendment, was aimed specifically and directly at the taxing of the bonds (including United States Liberty Bonds and Federal Farm Loan Bonds with which the major portion of the decision of the court is concerned); third, The Massachusetts taxing statute construed in the *Macallen case* did not impose a general tax on domicile, nor even a general income tax, but applied only to a special tax upon business corporations; fourth, the decision was definitely influenced by the fact that the courts of Massachusetts had already rejected the contention (now adopted by a majority of states, including Indiana) that an income tax was to be classified as an excise rather than a tax on property. (To this effect see: *Opinion of Justices,* 220 Mass. 613, 624, 108 N. E. 570; 266 Mass. 583, 585, 165 N. E. 900; *Harrison v. Commissioner of Corporations and Taxation,* 272 Mass. 422, 427, 172 N. E. 605, 71 A. L. R. 677).

(c). The decision of *Macallen Co. v. Massachusetts,* (1929), 279 U. S. 620 has been substantially overruled by the decision of *Pacific Co. v. Johnson,* (1932), 285 U. S. 480, and superseded by the Memorandum opinion affirming *New York ex rel. Northern Finance Co. v. Lynch,* (1933), 290 U. S. 601, affm: 262 N. Y. 477, 188 N. E. 27.

ARGUMENT.

PROPOSITION I.

The Tax Imposed by the Indiana Act Is a Tax Upon the Receipt of Gross Income, a Privilege Tax, and Does Not Burden Interstate Commerce in a Manner Forbidden by the Constitution.

Only the Validity of the Application of the Act is Involved in This Appeal.

By the express provisions of Section 6 (a) of Chapter 50 of the Indiana Acts of 1933 there is excepted from the gross income to be used as a measure of the privilege taxed, all of that gross income derived from business conducted in commerce between the State of Indiana and other states of the United States, or between Indiana and foreign countries, to the extent to which Indiana is prohibited from taxing by virtue of the Constitution of the United States. Therefore, no question of the constitutionality of the taxing Act is before this Court. The only question presented is the application of the Act to the specified factual situation reflected by the Record in this appeal, and consequently, the question is: Can the Act include within the measure of a tax based on income received by the appellant manufacturing corporation from sales where delivery was made to purchasers in other states;—or is such an application prohibited by the provisions of section 6 (a) of the Act and by sections 8 and 10, of article 1 of the Constitution of the United States? The issue is not the constitutionality of the statute, but the constitutionality of its application to a particular state of facts.

The Receipt of Income Within a State Is a Taxable Event.

In *The State of New York ex rel. Cohn v Graves, et al.*, (1937), 300 U. S. 308, 81 L. Ed. 366, this Court said at page 312:

> "That the *receipt of income* by a resident of the territory of the taxing sovereignty *is a taxable event* is universally recognized. *Domicile itself affords a basis for such taxation.* Enjoyment of the privileges of residence in the state and the attendant right to invoke the protection of its laws are inseparable from responsibility for sharing the costs of government." (Our italics.)

Later in the course of this opinion the Court said:

> "Neither the privilege nor the burden is affected by the character of the source from which the income is derived. *For that reason income is not necessarily clothed with the tax immunity enjoyed by its source.*"

The decision in *Maguire v. Trefry,* (1920), 253 U. S. 12, established the power of a state to tax a resident beneficiary on net income received from a trust established by a Pennsylvania testator. The trustee was a Pennsylvania trust company; the trust was being administered in that state; and the trust property, the income from which was in question, consisted of bonds of non-Massachusetts debtors which were held in Pennsylvania. The tax was sustained. The reasoning found in the decision is important as furnishing a direct clue to the court's conception of the factors relevant to these jurisdictional questions. The Court adopted the view of the Massachusetts court (see 230 Mass. 503, 102 N. E. 162) that the tax was based upon the protection received from

the state by the recipient of the income in his person, in his right to receive the income, and in its enjoyment;—in fine, that it was a return for the advantages received from the state, measured by income. The tax was held to be a proper one as a return for the advantages that domicile involves and confers.

The decisions establishing the right of a docimiliary state to tax the income received by one domiciled within it are a logical development of principles established with reference to property taxation. The consideration of one case of many will indicate the fact that the later income tax cases are in keeping with this development. *Southern Pacific Co. v. Kentucky,* (1911), 222 U. S. 63, held in connection with property taxes that a domiciliary state may tax tangibles which have not acquired elsewhere what is sometimes referred to as an "actual situs" predicable upon the requisite character and presence of physical jurisdiction. The result reached in this case, and the reasoning upon which it is based, should permit a domiciliary state to tax income under similar circumstances.

Domicile itself is affirmed to constitute a basis for taxation in *Lawrence v. State Board of Tax Commission,* (1932), 286 U. S. 276, 52 Sup. Ct. 556, 76 L. Ed. 1102, 87 A. L. R. 374. This decision is particularly important because it involved income which clearly could have been taxed by the non-domiciliary state in which it was earned. The basic assumption of the opinion is that responsibility for sharing the costs of government are inseparable from the enjoyment of the privileges of residence within a state and the concomitant right to invoke the protection of its laws. The economic interest realized by the receipt

of the income or represented by the power to control it at the domicile, and the fact that it was founded on the protection afforded the recipient in his person by the taxing state was deemed an adequate basis for imposing the tax. Jurisdiction to tax receipt of income is thus made dependent on the power of the taxing state to protect the person of the recipient generally, and specifically the receipt, enjoyment and control of the income at the place of domicile. In the opinion of the Court in this case this statement of the principles there established appears at page 279:

> "The obligation of one domiciled within a state to pay taxes there, arises from the unilateral action of the state government in the exercise of the most plenary of sovereign powers, that to raise revenue to defray the expenses of government and to distribute its burdens equably among those who enjoy its benefits. Hence, domicile in itself establishes a basis for taxation. Enjoyment of the privileges of residence within the state, and the attendant right to invoke the protection of its laws, are inseparable from the responsibility for sharing the costs of government. * * *
>
> "It is enough, so far as the constitutional power of the state to levy it is concerned, that the tax is imposed by Mississippi on its own citizens with reference to the receipt and enjoyment of income derived from the conduct of business, regardless of the place where it is carried on. The tax, which is apportioned to the ability of the taxpayer to bear it, is founded upon the protection afforded to the recipient of the income by the state, in his person, in his right to receive the income, and in his enjoyment of it when received. There are rights and privileges incident to his domicile in the state and to them the economic interest realized by the receipt of income or represented by the

> power to control it, bears a direct legal relationship."

The receipt of income within a state is a taxable event for the reason that the state of domicile protects by the extensive machinery of government its citizens and its corporations in the privilege of planning, producing, managing, creating, receiving, controlling and enjoying income. The conduct of the affairs of the appellant corporation under civilized rules is an exercise of the privilege of domicile within the state.

This Tax Is a Privilege Tax Imposed on the Receipt of Income.

In *Miles et al. v. Department of Treasury, etc., et al.*, (1935), 209 Ind. 172, 199 N. E. 372 at 378-379, 101 A. L. R. 1359, the Supreme Court of Indiana considered the constitutionality of Chapter 50 of the Indiana Acts of 1933 and had occasion to determine the exact nature of the Act presently before this Court. In holding that the tax was levied upon residents of the state upon the basis of the privilege of the receipt of income or domicile the Court said at page 188:

> "We conclude that the tax in question is an excise, levied upon those domiciled within the state or who derived income from sources within the state, upon the basis of the privilege of domicile or the privilege of transacting business within the state, and that the burden may reasonably be measured by the amount of income. The reasoning which justifies a tax upon the basis of domicile as readily supports and justifies a tax upon the basis of the right to receive income within, or transact business under the protection of, the state."

In 1936 the Indiana Supreme Court quoted, in its opinion in *Indiana Creosoting Co. v. McNutt, etc., et al.*, — Ind. —, 5. N. E. (2d) 310 at 313, the language from the *Miles* case which has been set forth, reaffirming its statement that the tax under consideration is a tax upon the basis of the privilege of receiving income, an incident of domicile of all residents of the State of Indiana.

Section 2 of the Act, the levying clause, levies the tax in a manner thoroughly consistent with this determination of the Supreme Court of Indiana relative to the exact nature of the tax, as witness the following pertinent excerpt:

> "Sec. 2. There is hereby imposed a tax, measured by the amount or volume of gross income, and in the amount to be determined by the application of rates on such gross income as hereinafter provided. Such tax shall be levied upon the entire gross income of all residents of the State of Indiana, and upon the gross income derived from sources within the State of Indiana, of all persons and/or companies, including banks, who are not residents of the State of Indiana, but are engaged in business in this state, or who derive gross income from sources within this state, * * *."
>
> Sec. 2, Chap. 50, Indiana Acts of 1933, pp. 388 at 390;
>
> 11 Burns' Indiana Statutes, 1933 Ed., 64-2602;
>
> Baldwin's Indiana Statutes, 1934 Ed., 15,982.

The express provisions of the Act in the section which levies the tax clearly indicates that the "measure" of the tax is the amount or volume of gross income received.

Likewise the title of the Act fully supports the determination of the Indiana Supreme Court as will be observed from the following:

> "An Act to provide for the raising of public revenue by imposing a tax upon the receipt of gross income to provide for the ascertainment, assessment and collection of said tax, and to provide penalties for the violation of the terms of this act, and declaring an emergency."
>
> Acts of Indiana 1933, page 388.

The Indiana Supreme Court in discussing the character of the tax involved in this appeal, in its decision in *Miles v. Department of Treasury, supra,* at page 187, said:

> "* * * The individual, as distinguished from his property, is protected in the enjoyment of the privileges of citizenship, the protection of his person, and the enjoyment of his income.
>
> "It cannot logically be said that one who engages in large enterprises, with the assurance that his rights are protected by the vast machinery of government which makes possible the conduct of affairs under civilized rules, has not enjoyed a privilege and protection, and put a burden upon the machinery of government on account of which he may be required to contribute to the governmental expense, merely because his activities did not yield him a net profit in any given period. The government must operate in years in which its citizens have not profited as well as in years in which they have. It is universally recognized that the burdens of government cannot be distributed with exact justice upon all persons and property. It is also recognized that to distribute the burden of government per capita would work an injustice upon those who are least able to pay and least able to cope with social and economic problems, in favor of those better equipped to meet social and economic problems, and who, because of their more complex activities, receive more protection from and put more burden upon the instrumentalities of government. * * *"

The Tax Is Not Upon a Selected Enterprise.

The exact character of the tax, insofar as the questions presented by the appellant manufacturing corporation on the Record are concerned, is that of a sharing of the costs of government as a return for the privileges of domicile and the receipt of gross income, including the concomitant right to protection; however, for a thorough understanding of the tax in its relation to the constitutional issue raised it is important to notice in addition its characteristics. Most fundamental of these is that the tax is not one aimed at business, or at a specified business. Neither is it a tax limited to certain types of business organizations. Its scope is general, in much the same sense that the state's *ad valorem* property taxes are general,—but to a greater degree, since gross income affords a broader base and therefore actively affects a greater number of persons. The term "general" has been used by this Court to designate systems of net income taxation which were extensive, though not universal, in that they exercised a common, public effect with relation to a majority of the individuals or companies within a state, and were not restrained or limited to a particular or specific import;—in exactly the same sense, this Act is general.

In *Miles et al. v. Department of Treasury, etc., et al.*, (1935), 209 Ind. 172, at 195, 199 N. E. 372, at 382, 101 A. L. R. 1359, it is said:

> "The law is intended to be general and to operate upon all residents of the state and all who derive revenue from sources within the state. * * *"

The tax in the instant case is not one levied only upon persons likely to be engaged in interstate commerce as were the taxes disapproved in *Galveston, H. and S. A. Ry.*

Co. v. Texas, (1908), 210 U. S. 217, 28 Sup. Ct. 638; or in *Crew Levick Co. v. Pennsylvania,* (1917), 245 U. S. 292, 38 Sup. Ct. 126; or in *Philadelphia and Southern Mail SS. Co. v. Pennsylvania,* (1887), 122 U. S. 326, 7 Sup. Ct. 1118. The Act, by its extensive application, indicates that it is not a device whereby the taxing state relieves domestic consumption, or confers on it any direct or indirect bounty, so that extra-state sources contribute more to the Indiana treasury than those whom that treasury directly serves. The decisions of this Court indicate that the extra-territorial effect of such special taxes, whether on property, franchises or privileges, is thought undue when the state of destination confines the tax to articles that come in from other states. We think that such restrained or specific taxes, limited in such a manner, would be equally undue if the state of origin were to confine its tax to articles destined for other states. Important then, is the factual observation that the tax now before this Court is not confined in either manner.

That this characteristic of being a tax general and extensive in nature, and not selective or limited, is important is indicated by the statement of Professor Thomas Reed Powell in 32 Harvard Law Review, 640:

> "All of the gross income taxes that have been declared unconstitutional have been levies on selected enterprises."

The reason for attaching special significance to the fact reported above is given by Professor Powell in the article entitled "State Income Taxes and the Commerce Clause," in 31 Yale Law Journal, 799 at 801, where he says:

> "When a statute picks out a special subject for a special tax, the object of its desire is practically certain to be forced into a generosity in excess of

> that indulged in by property and business generally. If this special subject is interstate commerce or includes interstate commerce, enterprise which straddles a state line is paying more than some or all of the enterprise that is of interest only to the taxing state. The danger that the taxing state will not heed the monition that charity beginneth at home is sufficient to justify the court in looking askance at any exaction on interstate commerce that is not certain to be matched by equivalent exactions on all local commerce.''

In the instances to which the appellant's brief refer us, it is of consequence to note that the court was not dealing with taxation that fell on all business or persons alike. It had before it the (grave possibility or) actuality of heavier burdens on interstate commerce than on other business. Where this possibility is foreclosed by general state taxation on all persons measured uniformly by all incomes received by citizens (and by all income received from business conducted within the state by non-residents), there is weighty reason for the contention that one domiciled in the state who exercises all of the major functions of domicile, —including the conducting of a complete manufacturing activity and receiving and controlling all of its income there,—should not be subsidized by an exemption from the payment of its pro rata share of the cost of government common to *all* business, merely because a part of the goods manufactured under the protection of the domiciliary state are delivered to purchasers in other states. In the instant case, the tax is not only on all business, but upon all persons domiciled within the state who derive income as the result of such domicile. The farmer, laborer, capitalist, professional man, business men of all kinds, and all persons, regardless of the activity which gives rise to the income, are equally affected.

There is No Discrimination.

Significant is it that one of the characteristics of this tax on the receipt of income is the fact that it operates upon all residents of the state, and all non-residents who derive revenue from business within the state, in exactly the same manner. The tax is measured by gross income generally; not by income from deliveries made outside of the state because of its source, but just in the same manner as the same measure is utilized with reference to one whose domicile is exercised exclusively in carrying on a purely intrastate enterprise. The rate of taxation does not vary as the result of business transactions having been completely carried out either within or without the state. In every instance, both the measure of the tax and the rate of taxation applied, will be identical in the conduct of any particular activity which is selected, regardless of whether the delivery of the goods is made to a purchaser within the boundaries of the State of Indiana, or to one located in a state other than Indiana. In the practical application of the Act we find no economic discrimination either against interstate commerce or in favor of local activities. The fact is, that the exaction sought to be made from the appellant manufacturing corporation measured by income received subsequent to delivery to another state is matched identically by an equivalent exaction on *all* local commerce.

In *Virginia v. Imperial Coal Sales, Inc.*, (1934), 293 U. S. 15, a capital tax was sustained when laid by the State of Virginia against the respondent, a (domestic) corporation having its principal office in Lynchburg, Virginia, and whose sole business was that of selling coal for foreign coal mining corporations. This Court said (at page 19):

"Property having its situs within the taxing state is not exempt from a non-discriminatory property tax merely because the property is used in interstate commerce. Corporations engaged in interstate commerce should bear their proper share of the burdens of the government under whose protection they conduct their operations, and non-discriminatory taxation of their property, although used in interstate commerce, as this Court has frequently said, affects that commerce only incidentally and is not inconsistent with the constitutional immunity from the imposition of direct burden."

In this case the Court pointed out that it was dealing with a property tax. However, the language quoted indicates clearly that the characteristic of being "non-discriminatory" is deemed one of the factors which is controlling. Of interest also is the statement that corporations engaged in interstate commerce should bear their proper share of the burdens of the government under whose protection they conduct their operations.

While the Court in *Virginia v. Imperial Coal Sales, Inc., supra,* was careful to distinguish between an ad valorem property tax and a privilege tax in relation to the question of whether the same is a burden upon interstate commerce, in the decision of *James, etc. v. The Dravo Contracting Company,* No. 3, October Term, 1937, Advance Sheets, page 13, it used the following significant language:

"The question of the taxability of a contractor upon the fruits of his services is closely analogous to that of the taxability of the property of the contractor which is used in performing the services. His earnings flow from his work; his property is employed in securing them. In both cases, the taxes increase the cost of the work and diminish his profits."

This language gives full recognition to the fact that after all a tax upon property is no less direct in its burden than is a tax upon gross receipts,—or measured by the gross receipts flowing from its use.

If there can be any reasonable doubt as to the proper inference to be drawn from the language quoted above, that doubt is removed by the Court at page 18, where it says:

> "But if it be assumed that the gross receipts tax may increase the cost to the government that fact would not invalidate the tax. With respect to that effect, a tax on the contractor's gross receipts would not differ from a tax on the contractor's property and equipment necessarily used in the performance of the contract. Concededly such a tax may validly be laid. Property taxes are naturally, as in this case, reckoned as a part of the expense of doing the work."

The accuracy of this statement cannot be successfully controverted. It follows then that a non-discriminatory general tax measured by gross income is in no different position than a non-discriminatory property tax on property utilized in interstate commerce. Since the Court has frequently said that a non-discriminatory ad valorem tax on property used in interstate commerce is not inconsistent with the constitutional immunity of such commerce from the imposition of direct burdens,

> *Virginia v. Imperial Coal Sales Co., Inc.,* (1934), 293 U.S. 15, 19,
> *Western Union Tel. Co. v. Taggart,* (1896), 163 U. S. 1,

the reasoning of the decision in *James, etc. v. The Dravo Contracting Company, supra,* justifies the conclusion that

a non-discriminatory tax using gross income as its measure would enjoy the same standing as an ad valorem property tax and hence could not be a direct burden in the constitutional sense.

In *Peck and Company v. Lowe,* (1918), 247 U. S. 165, 38 Sup. Ct. 432, 62 L. Ed. 1049, where the federal net Income Tax Act of October 3, 1913, was held not to impinge on clause 5 of section 9 of Article 1 of the Federal Constitution that "no tax or duty shall be laid on articles exported from any state," stress is put upon the fact that the tax questioned was "general" and upon the further fact that there was no discrimination. It is true that reference is made to the fact that the levy was upon the income net after all of the expenses were paid and losses adjusted; but it is equally true that a law which taxed the net income of persons engaged in foreign commerce, to the exclusion of all other persons, could not be upheld even if the levy were effective only after expenses were paid and losses adjusted. From this it would appear that the controlling fact was the non-discriminatory quality of the general tax. It is interesting to note the language used by the Court (247 U. S. 165 at 174):

> "The tax in question is unlike any of those heretofore condemned. It is not laid on articles in course of exportation or on anything which inherently or by the usages of commerce is embraced in exportation or any of its processes. On the contrary, it is an income tax laid generally on net incomes. And while it cannot be applied to any income which Congress has no power to tax (see *Stanton v. Baltic Mining Co., supra,* p. 113), it is both nominally and actually a general tax. It is not laid on income from exportation because of its source, or in a discriminative way, but just as it is laid on

> other income. The words of the act are 'net income arising or accruing from all sources.' There is no discrimination. At most, exportation is affected only indirectly and remotely. The tax is levied after exportation is completed, after all expenses are paid and losses adjusted, and after the recipient of the income is free to use it as he chooses."

Every test which is applied to the federal income tax in the above language, excepting that implied in the words "after all expenses are paid and losses adjusted" which we have already discussed, applies equally to the situation presented in the Act under consideration. Even the statement that "the recipient of the income is free to use it as he chooses" is applicable to the case under consideration. With these facts in mind, note what the Court says at page 175:

> "Thus what is taxed—the net income—is as far removed from exportation as are articles intended for export before the exportation begins. If articles manufactured and intended for export are subject to taxation under general laws up to the time they are put in course of exportation, as we have seen they are, the conclusion is unavoidable that the net income from the venture when completed, that is to say, after the exportation and sale are fully consummated, is likewise subject to taxation under general laws."

Then note the following:

> "In that respect the status of the income is not different from that of the exported articles prior to exportation."

Surely the status of the gross receipts from the sale is no more different from that of the exported articles prior to the exportation, than is net income. The status of gross

receipts by their very nature is much more akin to the status of the exported article for the reason that the net income can by no stretch of the imagination be regarded as the value of the article prior to exportation for the purposes of taxation.

Peck and Co. v. Lowe, supra, establishes the lack of discrimination as a practical test to be utilized in determining the impact of a taxing act with reference to the Constitution.

An interesting variant of the question of the existence of actual discrimination against interstate commerce is to be noted in connection with the *Ohio Tax Cases,* (1914), 232 U. S. 576, 34 Sup. Ct. 372. Before the decision of *Galveston, H. and S. A. Ry. Co. v. Texas,* (1908), 210 U. S. 217, 28 Sup. Ct. 638, the State of Ohio had a statute under which railroads were required to pay one per cent of their gross earnings from all commerce within the state. After the *Galveston* decision, the Ohio law was amended so that the gross receipts tax was limited to intra-state receipts, but the rate on railroads was increased from one per cent to four per cent. Such an act evidences a process of artificial selection which might effectively impose discriminatory burdens on interstate commerce. The Act now before the Court is non-discriminatory in that it provides for no higher rates with reference to those most likely to engage in interstate activities than with reference to those known to conduct a purely local business.

Indiana has no monopoly, natural or artificial, upon the production of road machinery. Consumption ratios change from year to year and doubtless will continue to do so. This tax on domicile and the receipt of gross income is not aimed at the business of manufacturing

as conducted by the appellant specifically, but that particular phase of manufacture is (as indeed manufacturing of all kinds is) subsumed in a general, non-discriminatory excise upon all who are domiciled within the state, or on non-residents who carry on business within the state, and who have gross income by which the tax may be measured. Since the Supreme Court's prohibitions have been directed mainly against discrimination against interstate commerce, this Act would appear not to be in conflict with the Commerce Clause of the Constitution.

Practical, Rather Than
Philosophical, Distinctions
Are to Be Recognized.

Mr. Justice Holmes in *Galveston, H. and S. A. Ry. Co. v. Texas,* (1908), 210 U. S. 217, at 225, 227, 28 Sup. Ct. 638 at 640, invites us to look to practical distinctions:

> "It being once admitted, as of course it must be, that not every law that affects commerce among the states is a regulation of it in a constitutional sense, nice distinctions are to be expected. Regulation and commerce among the states both are practical rather than technical conceptions, and, naturally, their limits must be fixed by practical lines.
>
> "It appears sufficiently, perhaps from what has been said, that we are to look for a practical rather than a logical or philosophical distinction. The state must be allowed to tax the property and to tax it at its actual value as a going concern. On the other hand, the State cannot tax the interstate business. The two necessities hardly admit of an absolute logical reconciliation. * * *"

The method of the practical approach recommended by Mr. Justice Holmes is undoubtedly responsible for two

recent realistic utterances of this Court. The first in the subordinating of the doctrinal to the common-sense view of the situation in the following statement from *James, etc. v. The Dravo Contracting Company, supra*:

> "The question of the taxability of a contractor upon the fruits of his services is closely analogous to that of the taxability of the property of the contractor which is used in performing the services. His earnings flow from his work; his property is employed in securing them. In both cases, the taxes increase the cost of the work and diminish his profits."

* * * * * * *

> "But if it be assumed that the gross receipts tax may increase the cost to the government that fact cannot invalidate the tax. With respect to that effect, *a tax on the contractor's gross receipts would not differ from a tax on the contractor's property and equipment necessarily used in the performance of the contract.*" (Our italics.)

The other statement is from *State of New York ex rel. Cohn v. Graves et al.*, (1937), 300 U. S. 308 at 312, 313. 81 L. Ed. 666 at 670:

> "That the receipt of income by a resident of the territory of the taxing sovereignty is a taxable event is universally recognized. Domicile itself affords a basis for such taxation. Enjoyment of the privileges of residence in the state and the attendant right to invoke the protection of its laws are inseparable from responsibility for sharing the costs of government."

And later:

> "Neither the privilege nor the burden *is affected by the character of the source* from which the in-

come is derived. For that reason *income is not necessarily clothed with the tax immunity enjoyed by its source.*" (Our italics.)

In *American Manufacturing Co. v. City of St. Louis,* (1919), 250 U. S. 459, 39 Sup. Ct. 522, an ordinance imposing an excise tax upon manufacturers to be measured or ascertained by all of their gross receipts was sustained despite the fact that some of the receipts had as their source the sale of the manufactured goods in states other than Missouri. This Court applied the rule of practicability and found the burden occasioned by the tax and its measure to be "only the same kind of incidental and indirect effect as that which results from the payment of property taxes or any other and general contribution to the cost of government. Therefore, it does not amount to a regulation of interstate commerce."

The State's Entire Taxing System Is to be Taken Into Account.

This Court has said that a practical line can be drawn by taking the whole scheme of taxation of the state into account.

> *Galveston, H. and S. A. Ry. Co. v. Texas,* (1908), 210 U. S. 217, 227, 28 Sup. Ct. 638, 640.

The Supreme Court of Indiana in its opinion in this cause,

> *Storen, etc., et al. v. J. D. Adams Manufacturing Co.,* (1937), — Ind. —, 7 N. E. (2d) 941 at 950;

pointed out that this Act and the Limitation of Tax Levies Act, (Chap. 237, Indiana Acts of 1933, pp. 1085 to 1090; Burns' Indiana Statutes, 1933 Ed., 64-301 to 64-306; Baldwin's Indiana Statutes, 1934 Ed., 15,892 to 15,896; were

enacted concurrently. Obviously, the scheme was to relieve all property, including that of the appellant, from what the Legislature considered a burden that bore too heavily upon the property, and to raise a sum equivalent to the resulting loss of revenues by broadening the tax base. The purpose of imposing the tax in question then, was not to increase the aggregate sum to be raised by all taxation within the state, but merely to readjust the taxing bases so that all who received benefits or potential benefits from government might pay what the legislature deemed their just proportion of the expenses of government.

In *Postal Telegraph Cable Co. v. Adams,* (1895), 155 U. S. 688, 697, 15 Sup. Ct. 268 this Court said:

> "By whatever name the exaction may be called, *if it amounts to no more than the ordinary tax upon property or a just equivalent therefor,* ascertained by reference thereto, it is not open to attack as inconsistent with the constitution." (Our italics.)

The same principle sustains the result reached in *Maine v. Grand Trunk Ry. Co.,* (1891), 142 U. S. 217; in *Ficklen v. Shelby County Taxing District,* (1908), 145 U. S. 1-22, 28 Sup. Ct. 638; *United States Express Co. v. Minnesota,* (1912), 223 U. S. 335, 32 Sup. Ct. 328, 56 L. Ed. 459; *Cudahy Packing Co. v. Minnesota,* (1918), 246 U. S. 450, 38 Sup. Ct. 373, 62 L. Ed. 827; *Pullman Co. v. Richardson,* (1923), 261 U. S. 330, 43 Sup. Ct. 366; and specifically a consideration of the entire taxing structure of the state seems to have led to the disapproval of the tax in *Galveston, H. and S. A. Ry. Co. v. Texas, supra.*

In *Pullman Company v. Richardson,* (1923), 261 U. S. 330, 43 Sup. Ct. 366, the Court said:

"In taxing property so situated and used a state may select and employ any appropriate means of reaching its actual or full value as part of a going concern,—such as treating the gross receipts from its use in both intrastate and interstate commerce as an index or measure of its value,—and if the means do not involve any discrimination against interstate commerce *and the tax amounts to no more than would be legitimate as an ordinary tax upon the property, valued with reference to its use, the tax is not open to attack as restraining or burdening such commerce.*" (Our italics.)

In most instances the volume of gross income received bears a far closer relation to the cost of governmental supervision than does the mere possession of property or a balance at the end of the fiscal year. A general, non-discriminatory tax with a gross receipts index, is but a method of distributing the cost of government, as readily as is a general ad valorem property tax or a general tax on net income. The Supreme Court of Indiana summarized the facts applicable in the statement in *Storen v. J. D. Adams Manufacturing Co.,* (1937), — Ind. —, 7 N. E. (2d) 941 at 950:

"* * * and, *since the total taxes collected were approximately the same as before,* it is obvious that property owners generally are paying no more in property and gross income taxes, but are paying less property taxes than formerly. It cannot be said that the tax is designed to or that it does, levy upon appellee and others engaged partly in interstate or foreign commerce more than their fair proportionate share of the expense of maintaining the government under which they conduct their business." (Our italics.)

The Tax in Question Imposes No Direct Burden on Interstate Commerce.

In view of the authorities heretofore cited, there is ample authority to support a tax in the nature of an excise upon the privilege of receiving gross income. Such a tax law enacted for the purpose of broadening the tax base and lowering the rate on tangible property being general in its application imposes no direct burden on interstate commerce.

In the case of *American Manufacturing Company v. St. Louis,* 250 U. S. 459, the city of St. Louis passed an ordinance levying against manufacturers a tax on the privilege of carrying on a business of manufacturers within the city in the amount of one dollar on each thousand dollars of sales made. In supporting this tax, the Supreme Court of the United States said:

> "We hold that the tax in question is a tax upon the privilege of pursuing the business of manufacturing these goods in the city of St. Louis; that when the goods were manufactured the obligation accrued to pay the amount of the tax represented by their production when it should be liquidated by their sale by the manufacturer; that their removal from the city of St. Louis and storage elsewhere, whether within or without the State, worked no change in this obligation; that their sale by the respondent wherever they may have been stored at the time, whether it was done through its home office in New York or the office of its factory in St. Louis, should have been reported in its return to the license collector of the city of

St. Louis and the amount included in fixing the amount payable on account of its license tax."

> *American Mfg. Co. v. St. Louis,* 250 U. S. 459, 462.

"The city might have measured such tax by a percentage upon the value of all goods manufactured, whether they ever should come to be sold or not, and have required payment as soon as, or even before, the goods left the factory. In order to mitigate the burden, and also, perhaps, to bring merchants and manufacturers upon an equal footing in this regard, it has postponed ascertainment and payment of the tax until the manufacturer can bring the goods into market."

> *American Mfg. Co. v. St. Louis,* 250 U. S. 459, 463, 464.

"In our opinion, the operation and effect of the taxing ordinance are to impose a legitimate burden upon the business of carrying on the manufacture of goods in the city; it produces no direct burden on commerce in the goods manufactured, whether domestic or interstate, and only the same kind of incidental and indirect effect as that which results from the payment of property taxes or any other and general contribution to the cost of government. Therefore, it does not amount to a regulation of interstate commerce."

> *American Mfg. Co. v. St. Louis,* 250 U. S. 459, 464.

The ordinance of the city of Saint Louis imposed a tax which, compared to the tax presently before the Court, was special in that it was on a selected enterprise while the tax here is general and extensive. In other respects

the differences between the Act and the ordinance are in form and not in practical operation.

Neither was designed nor intended as a regulation of, or a tax or burden upon, interstate commerce as such. Neither was designed nor intended as a discrimination against those engaged in interstate commerce. In each instance, exactions measured by gross receipts received as the result of deliveries of the manufactured articles to purchasers in other states was matched by an identically equivalent exaction on all gross income derived from sales where delivery was made within the State. The tax imposed by the City of St. Louis in the privilege of manufacturing goods imposed no burden on interstate commerce, and the case at bar imposes no undue burden.

American Manufacturing Co. v. City of St. Louis, (1919), 250 U. S. 459, 39 Sup. Ct. 552;

Hope Natural Gas Co. v. Hall, (1927), 274 U. S. 284, 288;

Flint v. Stone Tracy Co., (1911), 230 U. S. 107;

Home Insurance Co. v. New York, (1890), 134 U. S. 594;

U. S. Express Co. v. Minnesota, (1912), 223 U. S. 335, 32 Sup. Ct. 211;

Kansas City, F. S. and N. R. Co. v. Botkin, (1916), 240 U. S. 227, 60 L. Ed. 617, 36 Sup. Ct. 261;

Hump Hairpin Manufacturing Co. v. Emmerson, (1922), 258 U. S. 290, 66 L. Ed. 622, 42 Sup. Ct. 305;

Northwestern Mutual Life Insurance Co. v. Wisconsin, (1918), 247 U. S. 132, 38 Sup. Ct. 414.

The Rule Announced in James v. Dravo Assists in Determining This Case.

This Court has taken the position that the prohibition of taxes affecting the other sovereign member of our dual system of government to be more rigid than the restrictions upon the power of the states to impose taxes affecting interstate commerce.

> See: *Gillespie v. Oklahoma,* (1922), 257 U. S. 501, 505, 66 L. Ed. 338.

In view of the fact that the rule as to instrumentalities of the United States has been stated to be absolute in form and stricter in substance than the criteria applicable to the jurisdiction of the states to levy taxes which may in some manner affect commerce between the states, the recent decision of this Court holding a general, state-wide, non-discriminatory tax upon gross receipts (which because of the measure employed by both is similar to the tax upon domicile here questioned) was not a direct burden or encroachment upon the federal government and hence not an interference in the constitutional sense, is persuasive in establishing the principle that the tax on domicile measured by gross receipts and upon the receipt of gross income presently before this Court (which is general, state-wide, and non-discriminatory) is not a direct burden upon interstate commerce and hence not an interference with such commerce in the constitutional sense.

> See *James, etc. v. The Dravo Contracting Company,* (1937), — U. S. —, No. 3 October Term Advance Sheets page 13.

This Court in *James v. The Dravo Contracting Company, supra,* gave full recognition to the fact that after all, a tax upon property is no less direct in its burden than is a tax measured by the gross receipts flowing from its use.

> "With respect to that effect, a tax upon the contractor's gross receipts would not differ from a tax on the contractor's property and equipment necessarily used in the performance of the contract."

The Crew Levick Case Considered.

The appellant manufacturing corporation relies heavily upon certain quoted passages from the decision of this Court in *Crew Levick Co. v. Pennsylvania,* (1917), 245 U. S. 292, 38 Sup. Ct. 126, 62 L. Ed. 295. That case and the present one are readily distinguishable upon at least three important grounds: *first,* the question there presented was whether a duty was laid upon exports, or foreign commerce, contrary to the second paragraph of section 10 of article 1 of the Federal Constitution, and did not present any question under the Commerce Clause; *second,* the tax was upon a special, selected class, i. e., merchandisers,—a special class incidentally, most likely to be engaged in exporting and importing; *third,* the tax involved was *not* upon, or measured by, either gross income or gross receipts, but by an entirely distinct measure: the total volume of transactions whether income was ever realized upon the transaction or not. In essence

then, it was a selective *sales tax* upon those engaged in mercantile selling.

These distinctions are significant and should be considered further. The *first* is significant because it removes the case as an authority upon the interstate commerce question.

The *second* ground of distinction is important because the selection of the particular class most probable to be conducting foreign commerce justified the court in entertaining a suspicion that Pennsylvania intended to exact a contribution from the foreign merchandising business which was not matched by an equivalent exaction from all businesses conducted locally. In a sense, the very selection of this single, particular enterprise to be the sole object of the tax, under the peculiar circumstances of the case amounted to a form of discrimination. Under the Indiana Act every type of business, every form of business organization, every commercial enterprise is taxed, and taxed equally upon the same basis,—the generality or equality of the Act goes further than that: for not only is *all* commerce uniformly treated, but all individuals and associations even though not engaged in commercial activities are accorded a like usage. Whatever exaction results with reference to a particular type of business is matched by an equivalent exaction upon all other business, all other activities, and all other persons domiciled within the state. The factual situation is the direct antithesis of that presented in the *Crew Levick* case.

Third: In *United States Glue Company v. Town of Oak Creek*, (1918), 247 U. S. 321, 38 Sup. Ct. 499, 62

L. Ed. 1135, Ann. Cas. 1918 E, 748, this Court recognized the true nature of the tax dealt with in the *Crew Levick* case and characterized that tax as:

> "In *Crew Levick Co. v. Pennsylvania,* 245 U. S. 292, 38 S. Ct. 126, 62 L. Ed. 295, we held that a state tax upon the business of selling goods in foreign commerce, measured by a certain percentage of *the gross transactions* in such commerce, was by its necessary effect a tax upon such commerce, * * *" etc.

The Pennsylvania Act which formed the subject of the *Crew Levick* case indicated clearly that the criteria was the gross volume of business transacted as witness:

> "That . . . each retail vendor of or retail dealer in goods, wares and merchandise shall pay an annual mercantile license tax of $2, and all persons so engaged shall pay one mill additional on each dollar of the whole volume, gross, or business transacted annually. Each wholesale vendor of or wholesale dealer in goods, wares and merchandise shall pay an annual mercantile license tax of $3, and all persons so engaged shall pay one-half mill additional on each dollar of the whole volume, gross, of business transacted annually."

Whether income was ever actually realized was of no concern under the Pennsylvania Act,—the bare transaction, the naked sale, was sufficient to provoke the tax liability. The receipt, control or enjoyment of the fruits of the sale taxed were of no moment, since the tax was on the sale transaction regardless of whether any fruits were actually realized or not, and regardless of the presence or absence of any control or enjoyment of income. In essence the

Pennsylvania exaction was a *sales tax.* The tax upon domicile measured by the receipt of gross income resulting from that domicile here under scrutiny is much more than a sales tax in that it applies in a plethora of cases where there is no sale. For example, the receipt of interest, dividends, salaries, wages, commissions, income from the performance of services and contracts, are included in the index of the tax regardless of the utter absence of a sale. The *Crew Levick* decision relates to a sales tax. Such an exaction is not regarded as identical with gross income taxes, and the Supreme Court of Virginia is, therefore, representing the popular opinion when it holds that a tax on the sale is not an income tax.

> *Commonwealth v. Brown,* (1895), 91 Va. 762, 21 S. E. 357.

That the Court recognizes the difference between a sales and a gross income tax was recently indicated when this Court upheld a West Virginia tax upon occupations measured by gross income where the result was to increase the cost of the construction of a dam for the Federal government in the *James v. Dravo Contracting Company* case without feeling called upon to expressly overrule ***Indian Motorcycle Co. v. United States,*** 283 U. S. 570; ***Panhandle Oil Co. v. Knox,*** 277 U. S. 218; ***Graves v. Texas Co.,*** 298 U. S. 393,—three decisions in which the Court declared invalid a ***sales tax*** as applied to a vendor of goods to the other sovereign.

It is significant that the language which the appellants quote from the *Crew Levick* case and upon which they rely:

> "it operates to lay a direct burden upon every transaction in commerce by withholding, for the use of

the State, a part of every dollar received in such transactions,"

Crew Levick v. Pennsylvania, 245 U. S. 292 at 297,

is peculiarly applicable to a *sales or transaction tax;* but because the transaction is often history before any gross income is received and the bite of the tax takes effect, and indeed further because there is the distinct possibility that no income will be received, this language does not accurately describe a tax measured by the receipt of gross income. Of course this language was perfectly proper in the case which was before the Court because there the transaction or sale established the tax liability regardless of whether any income was realized or not.

That the language quoted should be limited to sales taxes is demonstrated by the fact that this Court has repeatedly indicated that there is nothing inherently bad in using gross receipts from interstate commerce as an index or measure of the value of property used in interstate commerce for the purpose of establishing a tax base if there is no discrimination against interstate commerce and the tax amounts to no more than would be legitimate as an ordinary tax upon such property.

Pullman Co. v. Richardson, (1923), 261 U. S. 330, at pp. 338, 339;

Cudahy Packing Co. v. Minnesota, (1918), 246 U. S. 450, at p. 453;

U. S. Express Co. v. Minnesota, (1912), 223 U. S. 335.

Note the language of the Court in *Pullman Co. v. Richardson,* (1923), 261 U. S. 330, at page 338, where the Court said:

> "In taxing property so situated and used a State may select and employ any appropriate means of reaching its actual or full value as part of a going concern,—such as treating the gross receipts from its use in both intrastate and interstate commerce as an index or measure of its value,—and if the means do not involve any discrimination against interstate commerce and the tax amounts to no more than what would be legitimate as an ordinary tax upon the property, valued with reference to its use, the tax is not open to attack as restraining or burdening such commerce."

Note also the language of the Court in *Cudahy Packing Co. v. Minnesota,* (1918), 246 U. S. 450, at page 453, where the Court said:

> "Of course, if it is laid on the earnings *as such,* they being derived largely from interstate commerce, it is an unconstitutional restraint or burden on such commerce and void. *Fargo v. Michigan,* 121 U. S. 230; *Philadelphia and Southern Steamship Co. v. Pennsylvania,* 122 U. S. 326; *Galveston, Harrisburg and San Antonio Ry. Co. v. Texas,* 210 U. S. 217. On the other hand, if what is done is to reach the property and not to tax the gross earnings, the *latter being taken merely as an index or measure of the value of the former, it well may be that the objection urged against the tax is untenable;* for, as this court has said, by whatever name the tax or taxes may be called that are fixed by reference to the value of the property, if they are not imposed because of its use in interstate or foreign commerce, and if they amount to no more than would be legitimate as an ordinary tax upon the property, valued

with reference to the use in which it is employed, they are not open to attack as restraining or burdening such commerce." (Our italics.)

The detailed analysis of the numerous cases cited in appellant's brief will result, we think, in unnecessarily lengthening this brief. It is sufficient to say that they fall into three general classes.

First, there are those which deal with receipts in the nature of tolls,—fares or freight charges by corporations engaged in the business of transportation or communication in interstate commerce. As to this class, *Philadelphia & S. M. S. S. Co. v. Pennsylvania,* 122 U. S. 326; *Leloup v. Port of Mobile,* 127 U. S. 640, and *Fisher's Blend Station Co. v. Tax Commission,* 297 U. S. 650, are fairly representative. It is sufficient to say as to that type or class that none of them are cases wherein the application of a general tax is considered. Moreover, under the Indiana Act, as administered, such receipts as are involved in said cases, are not made the measure of taxation.*

The cases are, therefore, not in point in any sense of the word and are not authority upon which to overthrow the Indiana Act.

The second class of cases is that class in which the court sustains a net income tax and in the course of the

* Regulation 140. Transportation and Communication.

"The gross receipts derived by railroads, interurbans, pipe line, bus and truck lines from carrying charges of passengers, including Pullman service on sleeping and dining cars, freight and telephone or telegraph messages originating in the State of Indiana, the destination of which is outside of the State of Indiana on a continuous conveyance or which originated outside the State of Indiana and terminated therein, will not be included in gross income tax returns." (R. 121.)

several opinions refers to the distinction between net income taxes and gross receipts taxes. We think that we have shown that these cases are likewise not authority for the overthrow of the Indiana Act insofar as the same applies to gross receipts from interstate commerce as a measure of the tax for the reason that all of them have to do with selected special classes and are not general taxes in the sense that the Indiana tax is a general tax, and for the further reason that the distinction in such cases between a net income tax as such a measure and a gross income tax, is more theoretical than actual, it appearing that there is, in fact, a very definite relationship between gross receipts and net profits.

The third class of cases is that type which is represented by the case of *Crew Levick Co. v. Pennsylvania*, 245 U. S. 292, wherein the question was squarely before the court as applied to foreign commerce, whether a tax upon a selected group, measured by gross transactions in interstate or foreign commerce, could be sustained. This, after all, we think, can fairly be assumed to be the case principally relied upon by the appellants. It is, however, easily distinguishable from the present case as heretofore set forth.

It is not an authority for the invalidation of the Indiana tax which is a general tax directed against all residents of Indiana and others who derive gross income from business transacted in Indiana. There is in the Indiana Act no discrimination between interstate and intrastate commerce *and no discrimination with respect to the selection of the class.* All are within the class. The real reason why lack of discrimination between interstate and intrastate commerce availed nothing in the Crew Levick case was

because there was discrimination in the selection of the class. But if the latter discrimination is removed, there can be no discrimination and, therefore, no burden except the indirect burden which falls upon every other taxpayer for the support of the government.

The burden imposed by the Indiana Act, insofar as it is a burden upon interstate commerce, is clearly indirect. It is the fitting in of one of the parts of a general scheme of taxation whereby the taxpayer is required to pay his proportionate share of the costs of government and is neither aimed at nor, in fact, taxes interstate commerce as such.

PROPOSITION II.

No Contract Having Been Made by Indiana to Exempt the Interest Received by Virtue of the Ownership of Bonds Issued by Municipal Corporations, the Inclusion of Such Interest in the Determinative Index of an Excise Tax Is Not an Impairment of Contract, and Not Repugnant to Section 10 of Article 1 of the Constitution of the United States.

The Exemption Was Not Contractual.

The appellant argues that the exemption of the bonds from property taxation by the provisions of section 5 of Chapter 59 of the Indiana Acts of 1919, is contractual, and impliedly works to exempt the interest derived from such bonds from being used as an index or measure for

an excise tax. It insists that when the bonds were issued the statutes then in force with reference to exemptions became a part of a statutory contract under which the bonds were issued and purchased. We do not believe it is necessary for this Court to determine whether or not the exemption is contractual, as will be shown later in this argument. We do say, however, that we cannot agree with statement of appellant's counsel.

In *East Saginaw Salt Mfg. Co. v. City of East Saginaw,* (1871), 13 Wall. 373, 20 L. Ed. 611, there was involved the constitutionality of a statute of the State of Michigan repealing a former act of the legislature of that state which provided in substance that all companies or corporations formed or that may be formed for the purpose of boring for and manufacturing salt should be entitled to have all their property, real and personal, used for the purposes mentioned in the act, exempt from taxation for any purpose. The act also provided for the payment of a bounty of ten cents for each and every bushel of salt manufactured by any individual, company or corporation, from water obtained from boring in the State of Michigan. It was argued on behalf of the salt company that the prior act held out an inducement or offer to induce parties to embark in the business of manufacturing salt in Michigan, and when such parties did subsequently engage in that business, and actually produce and manufacture salt, the act became a contract between the state and such parties, which a subsequent legislature could not constitutionally revoke or repeal.

The Supreme Court of the United States, after stating that it was within the power of the legislature to make

a valid contract exempting certain property from taxation, held that no such contract was created by the prior statute granting the exemption under consideration in that case. The Court said there was no consideration for the contract, and that there was no obligation on any person to comply with the conditions of the law. That it was purely voluntary on the one part and therefore purely voluntary on the other part;—that is, on the part of the legislature, to continue, or not to continue the law.

The Court further stated that the case differs entirely from the case of a charter granted to a private corporation. That in the case of a charter granted, powers and privileges are conferred by the state, and that if no right to alter or repeal is reserved, stipulations as to taxation, or as to any other matter within the power of the legislature, are binding on both parties.

The Court then went on to say that the Act of the legislature there under consideration could not be interpreted on that principle. That the Act was in its nature a *general law,* regulative of the internal economy of the state. That it merely granted a gratuity or bounty, and was therefore repealable at the desire or will of the legislature.

Again in *Grand Lodge of the State of Louisiana v. City of New Orleans,* (1897), 166 U. S. 143, 41 L. Ed. 951, the United States Supreme Court considered the constitutionality of a provision of the Constitution of Louisiana. There a prior act of the legislature had exempted a certain building (naming it in the act) owned by the Grand Lodge from taxation so long as it was occupied by the Grand Lodge. Subsequent to the enactment of that statute a new constitution was adopted by the state

containing a provision exempting from taxation property of charitable institutions, provided the property so exempted was not used or leased for purposes of private or corporate profit or income. The Supreme Court of the United States held that there was no consideration for the original enactment of the legislature exempting the entire building from taxation. That it was a mere bounty or a gratuity; and notwithstanding the recipients of such gratuity or bounty may have incurred expense upon the faith of the offer, the state is not bound thereby, and a subsequent legislature might constitutionally repeal such exemption.

Again in *Wisconsin and Michigan Railway Co. v. Powers*, (1903), 191 U. S. 379, 48 L. Ed. 229, there was involved the constitutionality of an act of the State of Michigan repealing an exemption from taxation granted to the railway company by a prior act of that state, on the ground that it impaired the obligation of a statutory contract. The alleged contract levied a tax upon railroads, but provided "that the rate of taxation fixed by this Act or any other law of this state shall not apply to any railway company hereafter building and operating a line of railroad within this state north or parallel 44 of latitude, until the same has been operated for the full period of ten years, unless the gross earnings shall equal $4,000.00 per mile," etc. The railroad company later built a road north of the line designated by the statute, and its gross earnings had never equaled $4,000.00 per mile, so that it would be entitled to the exemption if the earlier statute had not been repealed. The contention of the company was that a later act of the legislature, repealing the exemption above quoted, impaired the obligation of a

statutory contract, and thus violated Article 1, Section 10, of the Constitution of the United States.

The United States Supreme Court again held the repealing statute to be valid. In passing upon the question, the Court made this pronouncement:

> "In the case at bar, of course the building and operating of the railroad was a sufficient detriment or change of position to constitute a consideration if the other elements were present. But the other elements are that the promise and the detriment are the conventional inducements each for the other. No matter what the actual motive may have been, by the express or implied terms of the supposed contract, the promise and the consideration must purport to be the motive each for the other, in whole or at least in part. It is not enough that the promise induces the detriment or that the detriment induces the promise, if the other half is wanting. If we are to deal with this proviso in a general tax law as we should deal with an alleged simple contract, while, no doubt, in some cases between private persons the above distinctions have not been kept very sharply in mind. (*Martin v. Meles,* 179 Mass. 114, 117, 60 N. E. 397), it is clear that we should require an adequate expression of an actual intent on the part of the state to set change of position against promise before we hold that it has parted with a great attribute of sovereignty beyond the right of change."

And in *Shiner v. Jacobs,* 62 Iowa 392, N. W. 613, the Iowa Supreme Court was called upon to consider the constitutionality of an Act of the legislature of that state which reduced or altered the exemption from taxation of forest trees or timber exempted under a prior statute. The plaintiff contended that after the passage of the

prior act, he had planted some forty-seven acres of forest trees, complying with the provisions of the act as to the manner of planting and the manner of cultivating. The later act, he contended, was unconstitutional because it altered the amount or extent of the exemption granted by the prior act which was held out to him as an inducement to plant forest trees. The Supreme Court of Iowa said the exemption provided was an act of general legislation, and applicable to all prairie land in the state. That every owner of land was thereby invited to devote a part of his land to the culture of forest trees. That the law was not in the nature of a contract between the state and such land owners as availed themselves of its provisions, but more in the nature of an inducement or a gratuity. The Iowa Court said it had long been well settled that where an exemption from taxation is provided by the general laws of the state, any subsequent legislature may alter or remove the exemption. The Court also cited and quoted as authority, the case of *Salt Company v. East Saginaw, supra.*

In *Miller v. Hagemann,* 114 Iowa 195, 86 N. W. 281, an Act of the legislature provided that in all cities existing under special charter, having a population of more than 10,000, whenever any real estate may by ordinance be assessed with any special tax for the improvements of streets, then such real estate, so specially assessed, and the special assessment upon which shall be paid, shall after such payment be exempted from taxation for general road or street tax which might thereafter be assessed against it. The City of Davenport enacted an ordinance providing for an exemption authorized by the state statute. Later the legislature repealed its act authorizing the

exemption. The plaintiff then commenced an action to mandamus to compel the defendant, Treasurer of the City of Davenport, to give him credit for, and mark as discharged, a charge for district road taxes in that city. Plaintiff contended that the repealing statute was unconstitutional because it impaired the obligation of a contract created by the prior Act of the legislature, and the City Ordinance passed pursuant thereto.

The Supreme Court of Iowa in holding that there was no impairment of the obligation of a contract by the enactment of the repealing statute, said:

> "The power of taxation is one of the sovereign and necessary powers of government, and, although it has finally been settled, after much contention, that this power may be limited by the granting of exemptions which will, under the provisions of the federal constitution prohibiting the impairment of contract, be irrepealable if provided for in a valid contract made by the state,—as, for instance, where they are given as an incident to a grant of land upon a consideration, or are embodied in a charter contract,—yet the presumption is against any such surrender of the power of the state, and the exemption will be deemed repealable unless it clearly appears not only that the exemption is one which might be granted under the power of the state to contract, but also that it was clearly intended to be made irrepealable. This position is tersely stated in *Bank v. Billings,* 4 Pet., 514, 561, 7 L. ed., 939, 955, as follows: 'That the taxing power is of vital importance, that it is essential to the existence of government, are truths which it cannot be necessary to affirm. It would seem that the relinquishment of such a power is never to be assumed. We will not say that a state may not relinquish it; that a consideration sufficiently valuable to induce a par-

tial release of it may not exist; but, as the whole community has a right to insist that its abandonment ought not to be presumed in a case in which the deliberate purpose of the state to abandon it does not appear'."

Further, in the opinion, the Iowa Supreme Court, in citing many authorities including *East Saginaw Salt Co. v. City of East Saginaw, supra,* and *Grand Lodge of Louisiana v. New Orleans, supra,* said:

> "It is well settled that a general exemption from taxation, not embodied in a contract, is repealable, *even though property has been acquired or expenses incurred in reliance thereon.* Such an exemption is in the nature of a bounty, and not a contract, and 'those who rely upon it must base their reliance upon the free and voluntary good faith of the legislature'."

What is the nature of the exemption granted by Section 5 of Chapter 59 of the Indiana Acts of 1919? There was no consideration for the enactments of the exemptions therein contained. Those exemptions were granted by the legislature as a mere gratuity or bounty. True it is that the appellants have invested their money in municipal bonds. The appellants were not induced to invest their money in any particular business by any promise of the legislature that such statute would never be repealed. Nor was there anything contained in any of the statutes involved which could be construed as binding upon the State of Indiana.

This Court has often said that the power of taxation is one of the sovereign and necessary powers of government, and is inherent in the state. That its abandonment will never be presumed, in view of its vital importance and its

necessity to the existence of government. There is nothing contained in the statutes here under consideration upon which this Court could say that the legislature intended to exempt such property from taxation for all time to come. Nor is there anything in the act upon which this Court could base a construction that the legislature intended to say to investors "If you will invest your money in the types of bonds stated in these statutes, the State of Indiana promises and agrees not to tax them." There is nothing in the act upon which such a promise or agreement could even be inferred or presumed to have been made by the legislature. All the legislature did was to grant an exemption to those types of bonds without any statement or explanation as to how the exemption was being granted. As stated in *Wisconsin and Michigan Railway Co. v. Powers, supra,* the legislature was not making a promise, but framing a scheme of public revenue. It announced its policy, and possibly opened a chance for benefits to those who purchased the types of bonds indicated in the various statutes, *but it did not address them, and therefore it made no promise to them.*

A reading of *all* of the clauses or paragraphs of section 5 of Chapter 59 of the Indiana Acts of 1919 reveals clearly that the General Assembly of Indiana was engaged therein in announcing its policy,—and not holding out a specific offer to a group of investors.

The Existence of a Contract
Has Not Been Conceded.

The brief of the appellant contains two erroneous statements. The first of these is that "on appeal to the Supreme Court of Indiana, the appellees in their brief as-

sumed the existence of a contract of exemption from taxation, * * *." The appellees did not in the trial Court, in the Supreme Court of Indiana, and do not now in this appeal, concede the existence of a contract to exempt the bonds in question from taxation. There is nothing contained in the record at the pages indicated by the appellants (R. 38-40) wherein any statement has been made that the appellees specifically conceded the existence of the alleged contract. Contrariwise the following statement is to be found in the record at page 39:

> "It is submitted that *no contract has been made* by the State of Indiana not to include interest from bonds of state political subdivisions in the measure of excise taxes imposed by the state."

Reference to the appellant's complaint (R. 5 and 13-14) and to the note contained immediately after the statement of "Proposition 11" (R. 38) indicates that the reason for limiting the scope of the brief filed in the Supreme Court of Indiana to the question of whether or not the income from such municipal bonds could be included in the index of the excise tax in question, was because this was the *only* item with reference to such bonds which was in controversy in the trial court.

At page 42 of the appellant's brief the following statement appears:

> "The State Supreme Court in its opinion conceded the existence of the contract. It stated: 'The bonds from which the income was received are specifically exempted from taxation . . ." (R. 46).

This statement is erroneous in that it attempts to add to the decision of the Supreme Court of Indiana. That Court merely stated that the bonds in question were spe-

cifically exempted from taxation, but did not decide whether such exemption was or was not contractual. Since the claim for exemption made by the appellant in the original complaint filed in the trial Court specifically limits its title to such exemption to the grant contained "* by the statutes of Indiana in force now and at the time of the issuance of such bonds (being section 6 of an Act entitled 'An Act concerning taxation, repealing all laws in conflict therewith and declaring an emergency,' approved March 11, 1919 as amended by Chapter 191, Acts of 1923; Section 14037 Burns' Indiana Statutes 1926). (R. 5.)"; and since the Act is one granting exemptions from ad valorem property taxes as a matter of public policy, it is to be presumed that clause 20 of the section referred to is not of a nature entirely foreign to the other clauses contained in the said section, and therefore that such clause, relating as it does to municipal bonds, is to be construed as being a grant of immunity and not as being contractual.

The Supreme Court of Indiana did not determine whether or not section 14037 of Burns' Indiana Statutes 1926 edition was, or was not, contractual in nature. We do not believe that it was necessary for the Supreme Court of Indiana to determine this question, or that it is necessary for this Court to determine this question,—as will be fully developed later in this argument. We do say, however, that we cannot ~~agree with~~ the statement of appellant's complaint that the Supreme Court conceded the existence of the contract,—or that the appellees have conceded the existence of such a contract.

The Statutory Exemption Claimed is Applicable Only to Property Taxation.

The language employed by the General Assembly in Chapter 59 of the Indiana Acts of 1919 specifically indicates that the exemptions granted by section 5 are to apply to property taxation. That act dealt with the general property taxing system of the state. Section five, the one upon which appellant relies, opens with the statement:

> "The following *property* shall be exempt from taxation: * * *" (Our italics.)

It is well to note that the clause of section 5 of Chapter 59 of the Indiana Acts of 1919, relied upon by the appellant manufacturing company as forming the basis of its claim of exemption of interest is clause 20. There is nothing contained in this clause or paragraph which can be construed as an exemption of the *interest* derived from the bonds which are exempted thereby. The clause appellant relies upon follows:

> "The following *property* shall be exempt from taxation: (Our italics.)
>
> (Then follow 19 clauses or paragraphs listing property exempted.)
>
> "Twentieth. All bonds, notes and other evidence of indebtedness hereafter issued by the State of Indiana or by municipal corporations within the state upon which the state or the said municipal corporations pay interest shall be exempt from taxation."

Clause 20, Sec. 5, Chap. 59, Indiana Acts of 1919, p. 198 at p. 203;
11 Burns' Indiana Statutes 1933 Ed. 64-201;
Baldwin's Indiana Statutes, 1934 Ed. 15,518.

A study of all of the provisions of Chapter 59 of the Indiana Acts of 1919 indicates clearly that it deals with ad valorem property taxation exclusively. In addition, it is significant that the State of Indiana did not have any general tax measured by income in 1919 at the time that these grants of exemption were made, and did not have such a tax for many years thereafter,—until the Act presently before this Court was passed in 1933. These factors, together with the language quoted above, indicate that the exemption bounties granted were to be limited to the general ad valorem property tax system with which Chapter 59 of the Indiana Acts of 1919 deals.

> See: *Henry O. Hale, et al., v. Iowa State Board of Assessment and Review,* (Nov. 8, 1937), — U. S. —, 82 L. Ed., Advance Opinions 66 at 71.

This Court has recently indicated that grants of exemption must be shown by the claimant to have been indisputably within the intention of the legislature at the time that the section of the statute relied upon as granting an immunity from taxation was passed. In *Hale et al. v. Iowa State Board of Assessment and Review,* (November, 1937) 82 L. Ed. Advance Opinions, 66 at 71, we find the following statement:

> "The taxpayer in *Clyde v. Gilchrist* claimed the benefit of an exemption under a statute of New York to the effect that, upon payment of a recording tax, debts and obligations, secured by mortgages of real property should be exempt from other taxation by the state and local sub-divisions. The question was whether the exemption thus accorded was applicable to an income tax enacted long afterwards. The state court ruled against the taxpayer (*People ex rel. Central Union Trust Co. v. Wendell,* 197

App. Div. 131, 188 N. Y. S. 344; *People ex rel. Clyde v. Wendell,* 197 App. Div. 913, 187 N. Y. S. 949, 232 N. Y. 550, 134 N. E. 567), assuming the existence of a contract of exemption, but holding that it was not intended to apply to taxes upon income. This court, considering the fact that at the date of the exemption statute 'no one thought of an income tax,' and recalling that 'any contract of exemption must be shown to have been indisputably within the intention of the Legislature,' sustained the judgment of the state court. 'The conclusion does not seem to us very difficult to reach.' 262 U. S. at p. 98, 67 L. Ed. 893, 43 S. Ct. 501."

Nor can the allegation made by the appellant that the exemption granted by Sec. 14037 Burns' Indiana Statutes 1926 Edition, has a legislative history which indicates that it was, prior to 1919, a separate and distinct act, (being Ch. 179 of the Indiana Acts of 1903, p. 322) materially assist the appellant in its object of stretching the exemption granted from being a declaration of immunity from property taxation for the bonds themselves into a grant or bounty affecting the interest derived from the bonds and exempting the said interest from the impact of an excise tax measured by the receipt of gross income. The appellants have not shown, and it is submitted that they could not show, that the General Assembly of the State of Indiana of 1903 intended to grant a specific exemption from an excise upon the receipt of gross income to the interest in question. Indiana had no such tax in 1903. It had no such tax in 1919, when the legislature incorporated this section into an act granting numerous exemptions from ad valorem property taxation. No such tax was imposed in Indiana until 1933,—almost thirty years after the original passage of the section, the language of which, as con-

tained in the Acts of 1919, is relied upon by the appellant for title to the exemption claimed. It is interesting to note that the action of the General Assembly in 1919, in lumping the section referred to into Section 5 of Chapter 59 of the Indiana Acts of 1919, constituted a construction of the statute and an indication of the nature of the exemption by the legislature itself. In other words, the General Assembly, by the action taken in 1919, recognized the fact that the exemption, as originally conceived, was to apply only to ad valorem property taxes.

Legislative Intent to Treat Interest Unlike Bonds Was Affirmatively Expressed.

The identical act upon which the appellant manufacturing corporation bases its claim for privilege or exemption of interest contains within it internal evidence of a positive nature indicating that the General Assembly intended to, and did, treat interest separate and distinct from the bonds which it exempted;—and that this treatment was at variance with the immunity granted as a matter of state policy to the physical bonds themselves. Section 25 of the act upon which appellant relies (Chapter 59, Indiana Acts of 1919, p. 198 at p. 210) is as follows:

> "Where bonds or stocks are now or may hereafter be exempted from taxation, the accrued interest on such bonds or dividends on such stock shall be listed and assessed, unless otherwise exempted, without regard to the time when the same is to be paid."
>
> Sec. 25, Chap. 59, Indiana Acts of 1919, p. 198 at p. 210; 11 Burns' Indiana Statutes, 1933 Ed., 64-506; Baldwin's Indiana Statutes, 1934 Ed., 15,542.

This language is plain and leaves no room for construction. The *interest* derived from bonds which the act has exempted from the ad valorem property taxation, *is expressly made subject to such taxes.* The interest is specifically and expressly removed from the exemption accorded the property represented by the bond. It is ***not*** accorded the favor, or premium, or immunity that the act extends to the bonds as property. Therefore, there is no gratuity granted which prevents the State from taxing such interest;—and even if there had been sufficient consideration to make of the exemption granted a contract, still the provisions of Section 25, quoted above, are so definite in indicating that *interest is to be taxed* that we are driven to the conclusion that *no contract* has been made by the State of Indiana not to tax interest as property, or to exclude interest in the measure of an excise tax on receipt of gross income or the fruits of domicile imposed by the state. Since *no contract existed* preventing the inclusion of the interest in the determinative index of gross income, there was no impairment of the obligation of a contract because interest was subsumed in the gross income in question.

The Act Before This Court
Imposes An Excise
And Not a Property Tax.

The Indiana Supreme Court has characterized the tax in question as an excise levied upon those domiciled or deriving income from sources within the state in the case of *Miles, et al. v. Department of Treasury* (1935), 209 Ind. 172 at 188, 199 N. E. 372 at 379:

> "We conclude that the tax in question is an excise, levied upon those domiciled within the state

> or who derive income from sources within the state, upon the basis of the privilege of domicile or the privilege of transacting business within the state, and that the burden may reasonably be measured by the amount of income. The reasoning which justifies a tax upon domicile as readily supports and justifies a tax upon the basis of the right to receive income within, or transact business under the protection of, the state."

The tax is again designated as an excise, and not a property, tax in *Indiana Creosoting Co. v. McNutt, etc., et al,* — Ind. —, 5 N. E. (2d) 310 at 313, and the language set forth immediately above was again repeated.

Insofar as these decisions hold the tax in question not to be a property tax they follow the rule announced by the Indiana Appellate Court in *Owen v. Fletcher Savings and Trust Co.* (1934), 99 Ind. App. 365 at 376, 189 N. E. 173.

The opinion of the Indiana Supreme Court is in accord with that of the majority of states which have now reached the conclusion that an income tax is not a property tax.

State ex rel. Moon Co. v. Wisconsin Tax Comm. (1917), 166 Wis. 287, 163 N. W. 639;
Young v. Illinois Athletic Club (1923), 310 Ill. 75, 144 N. E. 369;
Standard Lumber Co. v. Pierce (1924), 112 Ore. 314, 228 Pac. 812;
Shaffer v. Carter (1920), 252 U. S. 37;
Hattiesburg Grocery Co. v. Robertson (1921), 126 Miss. 34, 88 So. 4;

State Ex rel. Knox v. Gulf, etc., R. R. (1925) 138 Miss. 70, 104 to 689;

O'Connell v. State Board (1934), 95 Mont. 91, 25 Pac. (2d) 114;

Lawrence v. State Tax Comm. (1932), 286 U. S. 276.

Since the tax forming the subject matter of this appeal is *not* a property tax, and since the exemption granted by the provisions of Chapter 59 of the Indiana Acts of 1919, as amended, extends an immunity *only* to the general ad valorem property tax, it follows that the interest from such bonds is not exempted from the excise tax here involved.

Appellant's Claim to Exemption Rests Solely on the Provisions of Clause 20 of Sec. 5, Ch. 59, Indiana Acts of 1919.

It is important to note that the record indicates that the only claim to an exemption made by the appellant in instituting this suit was founded upon Sec. 14037, Burns' Indiana Statutes, 1926 Edition, which is Clause 20 of Section 5, Chapter 59, Indiana Acts of 1919, p. 198 at 203. (R. 5.) The bonds forming the subject matter of this demand for exemption are described in the record in the following language:

> "* * * bonds, notes and other evidence of indebtedness issued by municipal corporations within the State of Indiana; all of which bonds, notes and other evidence of indebtedness bear interest, and by the statutes of Indiana in force now and at the time of the issuance of such bonds (being Sec. 6

of an Act entitled 'An Act Concerning Taxation, Repealing all Laws in Conflict Therewith and Declaring an Emergency, Approved March 11, 1919,' as Amended by Ch. 191, Acts of 1923; Sec. 14037 Burns' Indiana Statutes 1926) are declared to be exempt from taxation."

None of the bonds described in the footnotes numbered 23 and 24, appearing on page 45 of the Appellant's Brief, are shown by the record to have been owned by the appellant at the time of the trial, and no claim of exemption is based upon the ownership of any of such bonds. It is interesting to note that reference is made in these footnotes to county highway bonds, county library bonds and highway assessment bonds, none of which could be possibly included within the descriptive language of "bonds * * * issued by municipal corporations." It is further interesting to note that at least one type of bond described in footnote No. 24, i. e., Interstate Bridge Bonds, were the subject of legislative action exempting them from taxation in 1937, four years after the trial of this cause and the filing of the stipulation of facts appearing in the Record. The terms and exemption granted to any bond or other evidence of indebtedness not held by the appellant at the time of the trial can avail the appellant nothing in determining the scope of the exemption to be granted the appellant with respect to the bonds shown by the record to have been the subject matter of this litigation; and no exemption granted by the legislature after the trial of this cause to a type of bond not shown by the record to have been held by the appellant can be determinative in deciding whether or not the interest upon a different type of bond held by the appellant at the time of trial is or is not to be included in the index of an excise tax.

The Indiana Exemption Provision is Similar to Iowa Act Considered in Hale v. Iowa Board of Assessment, etc. (1937).

Insofar as the question is presented as to whether an exemption statute containing such language as: *"The following property shall be exempt from taxation"* (Sec. 5, Chap. 59, Indiana Acts of 1919, p. 198 at p. 199) applies to excise taxes as well as property taxes, it is well to note that this language is cognate to that used in the Iowa exemption statute reviewed in *Henry O. Hale etc. v. The Iowa State Board of Assessment and Review* (1937), 82 L. Ed., Advance Opinions 66, which was: *"The following classes of property are not to be taxed."* (Sec. 1304 of the Code of Iowa 1907.) In the case reviewed by this Court, the Iowa Supreme Court had, in a previous decision, announced that the exemption granted was to be limited to property taxes. See: 271 Northwestern Reporter 168. This construction of the Iowa exemption provision by the Iowa Supreme Court was accepted by this Court in the *Hale* decision. Because of the marked similarity of the language employed in the Indiana and Iowa acts, we will refer briefly to other decisions which have construed this provision of the Iowa act, or related or parallel provisions.

In the case of *Sioux City v. School District* (1880), 55 Iowa, 150; 7 N. W. 488, it was held that the exemption contained in Section 797 of the Code of 1873 *applied to general property taxes* and not to a special tax such as an assessment for street improvements.

In the case of *Edwards & Walsh Construction Company v. Jasper County* (1902), 117 Iowa, 305; 90 N. W. 1006, it was held that the provision of the statute which exempted the property of a county devoted entirely to public use did not apply to special assessment for street improvements, *but only to a general property tax.*

Again in *Iowa Mutual Tornado Ins. Assn. v. Gilbertson, State Treasurer, et al.* (and seventeen other cases) (1906), 129 Iowa, 658; 106 N. W. 153, The Supreme Court of Iowa said that the exemption from taxes of the property of religious, charitable and educational institutions granted under Section 1304 of the Code of 1897 (being the same as Section 6944 of the Code of 1935) did not grant an exemption from a business or license tax, *but only general property taxes.*

In *State of Iowa v. City of Des Moines, et al.* (March 17, 1936) 266 N. W. 41 (not yet reported in Iowa reports), the Supreme Court of Iowa followed its prior holdings and said that a similar exemption provision has no application to an excise tax but only to a property tax.

The Iowa Supreme Court is not the only one that has passed on this question. Numerous other states have been called upon to determine whether or not a general constitutional or statutory provision exempting property of a state, county or municipal corporation, including bonds, from taxation, applies only to general property taxes, or whether it also applies to an excise tax. Quite generally the Courts have held that such a constitutional or statutory exemption applies only to general property taxes. Some of the cases which may be relied upon in support of the proposition are:

City of Portland v. Kozer, 108 Ore. 375; 217 Pac. 833;

Crockett v. Salt Lake County, 72 Utah 337; 270 Pac. 142;

Independent School District v. Pfost, 51 Idaho 240, 4 Pac. (2d) 893; 84 A. L. R. 820;

City of Ardmore v. State of Oklahoma, 32 Pac. (2d) 728;

Oregon v. Preston, 103 Ore. 631; 206 Pac. 304;

State v. City of Sioux Falls, 60 S. Dak. 330, 244 N. W. 365;

State v. Board of Commissioners of Barton County, Kansas (1935), 51 Pac. (2d) 33.

In *Van Dyke v. Wisconsin Tax Commission* (March 5, 1935), 217 Wis., 528; 259 N. W. 700, the Supreme Court of Wisconsin had before it practically the same question with which this Court is confronted. The question was whether or not interest from county road bonds was subject to an income tax. The statute under which the bonds were issued became a law of Wisconsin on June 15, 1911. Section 1317M-12 provided as follows:

> "Any county, if its board shall so determine, may raise money for original improvement of any portion of the system of prospective highways by *issuing non-taxable,* four per cent, semi-annual interest payment bonds, running not more than ten years, and not exceeding with all other county indebtedness, the constitutional limit, the money to be expended in the respective towns in portions determined by the County Board according to Section 1317M-5; such bonds to be in such form as the State Highway Commission shall approve, and not to be sold at less than par * * *" (Our italics.)

In 1919, sweeping changes were made in the highway

laws and the section just quoted was repealed along with other laws, but was immediately re-enacted in Chapter 337 of the Acts of 1919. After the enactment of the Chapter 337 of the laws of 1911, the legislature enacted Chapter 516 exempting from taxation bonds issued by any county, town, city, village, school district, etc., in that state. Shortly after the enactment, the legislature enacted Chapter 658 of the laws of 1911 providing for an income tax. The question then was whether or not the exemptions granted by Chapters 337 and 516 of the laws of 1911 was an exemption from property tax or from all taxes.

In passing on the question, the Court made this statement:

> "It seems clear to us that at the time Chapter 337, Laws of 1911, was enacted, the only taxation to which such bonds could have been subjected was personal property taxation. Applying the reasoning here that was applied to the first contention relating to municipal bonds, and taking into consideration the fact that all of these acts were considered by the same Legislature, it seems clear that the Legislature, when it authorized the issuing by counties of nontaxable bonds, intended that such bonds should be free from personal property taxation only. Had the income tax law not been subsequently enacted, no one would contend that Chapter 337 did anything more, or was intended to do anything more, than exempt such bonds from taxation as personal property."

People v. Gilchrist,
262 U. S. 94, Sustains
Appellees' Position.

In addition to the *Hale* case, this Court has decided at least one other case which, we believe, sustains appel-

lees' contention. Although the question of interest from tax-free state bonds was not involved, yet the legal proposition there raised and decided was analogous. In that case the question was whether or not the interest from certain bonds secured by mortgages was exempt from the income tax of New York State, because of the provision in the recording statute of that state, pursuant to which statute the mortgages were recorded, that debts and obligations secured by such mortgages shall be exempt from other taxes by the state and local subdivisions. This Court, in passing upon the question held that the interest was returnable for state income tax purposes and that the mortgage recording statute granting the exemption pertained only to a tax on the bonds, and not to an income tax, saying:

> "A tax upon the individual, measured by net income, might be regarded as one step removed from a tax on the capital from which the income was derived."

Macallen v. Massachusetts,
279 U. S. 620 Is Not
Applicable.

The appellant places much reliance upon the opinion of this Court expressed in *Macallen v. Massachusetts* (1929), 279 U. S. 620, 73 L. ed. 874. There are certain noticeable distinctions between the Macallen case and the present appeal.

First. The Massachusetts statute creating the exemption involved in the *Macallen* case is introduced by the language: *"Persons and Property exempt from taxation."* The statute then reads: "Section 5. The following

property and polls shall be execpt from taxation." In other words that statute exempted not only property, *but persons,* as well. The Indiana statute specifically refers to property and does not mention persons in any manner. (Our italics.)

Second. The Indiana Act contains internal evidence that interest is to be dealt with in a *wholly different manner* than the bonds as property. The interest was specifically made taxable under the Indiana Act. (See Section 25, Chapter 59, Indiana Acts of 1919, p. 198 at p. 210.)

Third. Under the Massachussetts statutes, as originally enacted, income from tax exempt securities was exempted from the tax. By the amendment which resulted in the *Macallen* case the legislature removed this exemption. The result of this amendment was to single out and to impose a tax on this interest alone. It was aimed directly at the persons holding tax free bonds. It was not a case of taxing all persons, or even all income.

Fourth. The Massachusetts taxing statute construed in the *Macallen* case did not impose a general or extensive tax upon all who were domiciled within the state or who transacted business there, but was levied selectively on business corporations alone.

Fifth. The decision of the Supreme Court in *Macallen v. Massachusetts* was definitely influenced by the construction which the highest Court of the State of Massachusetts had placed upon the Act. The Courts of Massachusetts had, prior to this case, already rejected the contention (which is now adopted by a majority of the states including Indiana) that an income tax was to be classified as an

excise rather than a tax on property. To this effect see *Opinion of Justices,* 220 Massachusetts 613, 624, 108 N. E. 570, 266 Mass. 583, 585, 165 N. E. 900; *Harrison v. Commissioner of Corporations and Taxes,* 272 Mass. 422, 427, 172 N. E. 605, 71 A. L. R. 677.

It is true that the *Macallen* case is often cited for the proposition that interest from tax free securities cannot be included in the gross income of a corporation under a statute imposing a franchise tax on a corporation, measured by its net income. That this was never the intention of the Court in the *Macallen* case is definitely and convincingly shown by a reading of the opinions in *Pacific Company v. Johnson,* 285 U. S. 480, and *Educational Films Corp. v. Ward,* 282 U. S. 379.

Northwestern Ins. Co. v. Wisconsin, 275 U. S. 136, is Not Applicable.

The appellant relies heavily upon the opinion of this Court expressed in *Northwestern Insurance Company v. Wisconsin,* (1927) 275 U. S. 136. The question of the impairment of the obligation of a contract within the purview of Section 10 of Article 1 of the Constitution was not presented in that case. That case dealt with the taxing by the State of Wisconsin of interest on bonds issued by the United States of America,—an entirely different question. For this reason the decision does not indicate the criteria to be applied in determining whether or not a state has entered a statutory contract to exempt interest from bonds; nor does the case lay down any rule applicable to the determination of the extent of immunity from taxation granted as a matter of state policy to bonds issued by its municipal subdivisions. The language of the act quoted

by the appellant at page 47 of its brief indicates very clearly that this case was decided upon the authority of *Gillespie v. Oklahoma,* 1922, 257 U. S. 491. That case announced the rule that:

> "The rule as to instrumentalities of the United States on the other hand *is absolute in form* and at least stricter in substance." (Our italics.)

The prohibition from taxing the other sovereign member of our dual system of Government must be, and is, rigid. For this reason, and in view of the fact that a contract to exempt interest was never entered into by the State of Indiana, it is apparent that the *Northwestern Insurance Co. v. Wisconsin* decision, while authoritative in establishing the absolute immunity of Federal bonds and their interest from taxes, is not applicable to the facts presented by the record in this appeal.

No Contractual Inhibition to Exclude Interest Existed at the Time of this Trial.

The attention of the Court is directed to the fact that the appellant in the complaint filed in the Marion Superior Court rested its claim to exemption upon the provisions of section 14037 Burns' Indiana Statutes 1926 Edition (now contained in 11 Burns' Indiana Statutes, 1933 ed. 64-201). (R. 5.) It is significant that the section relied upon by the appellant opens with the following language:

> "The following *property* shall be exempted from taxation." (Our italics.)

In the same act containing the section upon which appellant relies, we find internal evidence of a positive

nature indicating that the General Assembly intended to, and did, treat the interest derived from bonds in a wholly separate and distinct manner from the bonds which that act exempted. In other words, in the same act, we find a section which indicates that the immunity granted as a matter of state policy to the physical bonds themselves is not, upon any consideration, to be extended to the interest derived from such bonds. Section 25 of the Act upon which appellant relies is as follows:

> "Where bonds or stocks are now or may hereafter be exempted from taxation, *the accrued interest on such bonds or dividends on such stock shall be listed and assessed,* unless otherwise exempted, without regard to the time when the same is to be paid." (Our italics.)
>
> Sec. 25, Chap. 59, Indiana Acts of 1919, p. 198 at p. 210; 11 Burns' Indiana Statutes, 1933 Ed., 64-506; Baldwin's Indiana Statutes, 1934 Ed., 15,542.

CONCLUSION.

In view of the foregoing, the decision of the Supreme Court of the State of Indiana should be affirmed.

Respectfully submitted,

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February 28, 1938.

APPENDIX "A"

Chapter 50, Acts of Indiana General Assembly, 1933, Acts of 1933, p. 388.

AN ACT to provide for the raising of public revenue by imposing a tax upon the receipt of gross income, to provide for the ascertainment, assessment and collection of said tax, and to provide penalties for the violation of the terms of this act, and declaring an emergency. (H. 513. Approved February 27, 1933.)

Section 1. *Be it enacted by the general assembly of the State of Indiana,* That this act may be cited as the "Gross Income Tax Act of 1933."

(a) When used in this act, the term "person" or the term "company" herein used interchangeably, includes any individual, firm, copartnership, joint venture, association, corporation, municipal corporation, estate, trust, or any other group or combination acting as a unit, and the plural as well as the singular number, unless the intention to give a more limited meaning is disclosed by the context. * * *

* * * (f) The term "gross income," except as hereinafter otherwise expressly provided, means the gross receipts of the taxpayer received as compensation for personal services, and the gross receipts of the taxpayer derived from trades, businesses or commerce, and the gross receipts proceeding or accruing from the sale of property, tangible or intangible, real or personal, or service, or any or all of the foregoing, and all receipts by reason of the

investment of capital, including interest, discount, rentals, royalties, fees, commissions or other emoluments, however designated, and without any deductions on account of the costs of property sold, the cost of materials used, labor cost, interest or discount paid, or any other expense whatsoever, and without any deductions on account of losses; *Provided, however,* That the term "gross income" shall not include cash discounts allowed and taken on sales; nor freight prepaid by the taxpayer and repaid to him by the purchaser; goods, wares or merchandise, or the value thereof, returned by customers when the sale price is refunded either in cash or by credit; nor the sale price of any article accepted as part payment on any new article sold, if and when the full sale price of the new article is included in the "gross income" subject to taxation under this act; *Provided, further,* That "gross income" shall include the proceeds from the sale of any property handled on consignment by the taxpayer * * *

* * * Sec. 2. There is hereby imposed a tax, measured by the amount or volume of gross income, and in the amount to be determined by the application of rates on such gross income as hereinafter provided. Such tax shall be levied upon the entire gross income of all residents of the State of Indiana, and upon the gross income derived from sources within the State of Indiana, of all persons and/or companies, including banks, who are not residents of the State of Indiana, but are engaged in business in this state, or who derive gross income from sources within this state, and shall be in addition to all other taxes now or hereafter imposed with respect to particular occupations and/or activities. Said tax shall apply to, and shall be levied and collected upon, all gross incomes received on

or after the first day of May, 1933, with such exceptions and limitations as may be hereinafter provided.

Sec. 3. The tax hereby provided for shall be imposed at the following rates:

(a) Upon the entire gross income of every person engaged in the business of manufacturing, compounding, or preparing for sale, profit, or use, any article or articles, substance or substances, commodity or commodities; or in the business of mining and/or producing for sale, profit, or commercial use any oil, natural gas, stone, coal, sand, gravel or other mineral product, or felling and producing timber, for sale, profit or commercial use; or in agriculture, including the production of live stock, poultry, eggs, or any other product of the farm, orchard, garden or greenhouse, one-fourth of one per cent.

(b) Upon the entire gross income of every person engaged in the business of wholesaling and/or jobbing tangible commodities not specifically mentioned in subsection (d) of this section, one-fourth of one per cent.

(c) Upon the entire gross income of every person engaged in the business of retailing of any tangible commodity or commodities not specifically mentioned in subsection (d) of this section, one per cent.

(d) Upon the entire gross income of every person engaged in the business of producing, transmitting, wholesaling and/or retailing electrical energy; or producing, transporting, wholesaling and/or retailing artificial gas, or mixtures of artificial and natural gas; operating a steam and/or electric railway, street car line, motor vehicle, steam or motor boat, or any other vehicle for the transportation of freight, express and/or passengers for hire;

operating a pipe line for the transportation of any commodity for hire; operating any telephone and/or telegraph line; operating any water or sewerage system; or operating any other utility not expressly provided for elsewhere, one per cent.

(e) Upon the entire gross income of every person engaged in the business of operating any bank, trust company, building and loan association, insurance or casualty company, finance company, small loan company, or any other business of a similar nature, one per cent.

(f) Upon the gross income of every person engaged in any business or activity not enumerated in subsections (a) to (e) inclusive, of this section, including, but not in limitation of the foregoing, the gross income from professional services, personal services, sales of real estate, all funds received for the performance of contracts, all funds from the investment of capital, and all receipts from any source whatsoever, one per cent. * * *

* * * Sec. 6. There shall be excepted from the gross income taxable under this act:

(a) So much of such gross income as is derived from business conducted in commerce between this state and other states of the United States, or between this state and foreign countries, to the extent to which the State of Indiana is prohibited from taxing under the Constitution of the United States of America. There shall also be excepted from such gross income, salaries, pensions, and other emoluments paid by the United States of America or any of its agencies, and interest or other earnings paid upon bonds or other securities issued by the United States of America or its agencies, to the extent that the State of Indiana is prohibited from imposing a tax upon

such salaries, pensions, emoluments, interest, and/or earnings, by the Constitution of the United States of America.

(b) All taxes received or collected by the taxpayer as agent for the State of Indiana and/or the United States of America.

(c) So much of such gross income as is derived from sales to the United States government, its departments, or agencies, to the extent to which the State of Indiana is prohibited from taxing under the Constitution of the United States of America.

(d) Amounts received under life insurance policies and contracts paid by reason of the death of the insured.

(e) Amounts received, other than amounts paid by reason of the death of the insured, under life insurance endowment or annuity contracts, either during the term, or at maturity, or upon surrender of the contract, but in no case in excess of the total amount of the premiums paid upon such contracts. * * *

* * * Sec. 15. The tax imposed by this act shall be in addition to all other licenses and taxes imposed by law as a condition precedent to engaging in any business taxable hereunder, except as in this act otherwise specifically provided. But no municipality shall be authorized to levy any tax by virtue of the provisions of this act. * * *

* * * Sec. 29. If any clause, sentence, paragraph or part of this act shall for any reason be adjudged to be invalid, by any court of competent jurisdiction, such judgment shall not affect, impair, or invalidate the remainder of this act, but shall be confined in its operation to the clause, sentence, paragraph, or part thereof directly involved in the controversy in which such judgment shall have been rendered.

APPENDIX "B"

Burns' Indiana Statutes Annotated, 1926 Ed., Sec. 14-037.

Burns' Indiana Statutes Annotated, 1933 Ed., Sec. 64-201.

"The following property shall be exempt from taxation:"

(Then follow nineteen clauses enumerating specific exemptions.)

"Twentieth. All bonds, notes and other evidence of indebtedness hereafter issued by the State of Indiana or by municipal corporations within the state upon which the said state or the said municipal corporations pay interest shall be exempt from taxation.

Twenty-first. All bonds hereafter authorized by any county or township in the state of Indiana for the purpose of building, constructing and paying for the construction of any free gravel, macadamized or other improved roads, shall be exempt from taxation: Provided, Said bonds shall not bear a greater rate of interest than five (5) per cent interest per annum, payable semiannually.

Twenty-second. All bonds and other evidences of indebtedness hereafter issued by or in the name of any municipality or other political or civil subdivision of the State of Indiana, or by or in the name of any taxing district in the State of Indiana, for the purpose of paying the cost of acquisition, construction, improvement or maintenance of streets, highways, drains, levees, parks, docks, waterways, boulevards, playgrounds, bridges, sewage-disposal plants and other improvements of public benefit

and which bonds or other evidences of indebtedness are payable from special assessments or special taxes, shall be exempt from taxation, unless otherwise expressly provided in this section.

Twenty-three. All property both real and personal and all bonds, notes, mortgages and other evidence of indebtedness heretofore or hereafter issued and negotiated by the Indiana state board of agriculture pursuant to the provisions of any statute shall be exempt from taxation.

Twenty-fourth. All real estate and personal property used exclusively by the Indiana national guard or any other military organization of the state for armory purposes, shall be exempt from taxation so long as the same is used exclusively for such purposes.

Twenty-fifth. All property whether real or personal owned or held for the use of corporations, not for profit, which are organized for the purpose of discovering and preventing fires and saving property and life from conflagration.

Twenty-sixth. All annuities payable by religious or charitable organizations, or by educational institutions located in this state, to any person or persons who have made gifts, bequests or devises to any such organization or institution and which shall have been accepted for the purposes of such organization or institution under the provisions of any law of this state. (Acts 1919, ch. 59, 5, p. 198; 1920 (Spec. Sess.) ch. 49, 1, p. 164; 1921, ch. 222, 6, p. 638; 1923, ch. 191, 1, p. 558.)

Burns' Indiana Statutes Annotated, 1926 Ed., Sec. 14-065.

Burns' Indiana Statutes Annotated, 1933 Ed., Sec. 64-506.

"Where bonds or stocks are now or may hereafter be exempted from taxation, the accrued interest on such bonds or dividends on such stocks shall be listed and assessed, unless otherwise exempted, without regard to the time when the same is to be paid.". (Acts 1919, ch. 59, sec. 25, p. 198.)

APPENDIX "C"

Chapter 237.

AN ACT relating to tax levies and providing for the fixing thereof, limiting the amount of the same and repealing all laws in conflict therewith, and declaring an emergency.

[S. 319. Approved March 9, 1933.]

Section 1. *Be it enacted by the general assembly of the State of Indiana,* That the total of all tax levies whether fixed by the state board of tax commissioners or by statute from which any revenue shall accrue or be paid to the state treasury for any purpose or for the use of any fund kept or received by the treasurer of state, for the year 1933, upon which taxes are payable in the year 1934 and for each year thereafter shall not exceed the sum of fifteen cents upon each one hundred dollars of taxable property within said state.

Sec. 2. The term municipal corporation, as used herein shall include counties, townships, school townships, cities, school cities, towns, school towns, school districts, sanitary districts, park districts and all taxing units within the state.

Sec. 3. The total of all tax levies on property within any municipal corporation for all municipal corporations for which the property therein is taxable, except as provided in section 4 of this act, shall not exceed the following total rates:

In territory outside of the corporate limits of incorporated cities and towns, the total tax rate for all purposes, including the state levy referred to in section 1 of this act, shall not exceed one dollar on each one hundred dollars of taxable property therein.

In territory inside of the corporate limits of incorporated cities and towns, the total tax rate for all purposes, including the state levy referred to in section 1 of this act, shall not exceed one dollar and fifty cents on each one hundred dollars of taxable property therein.

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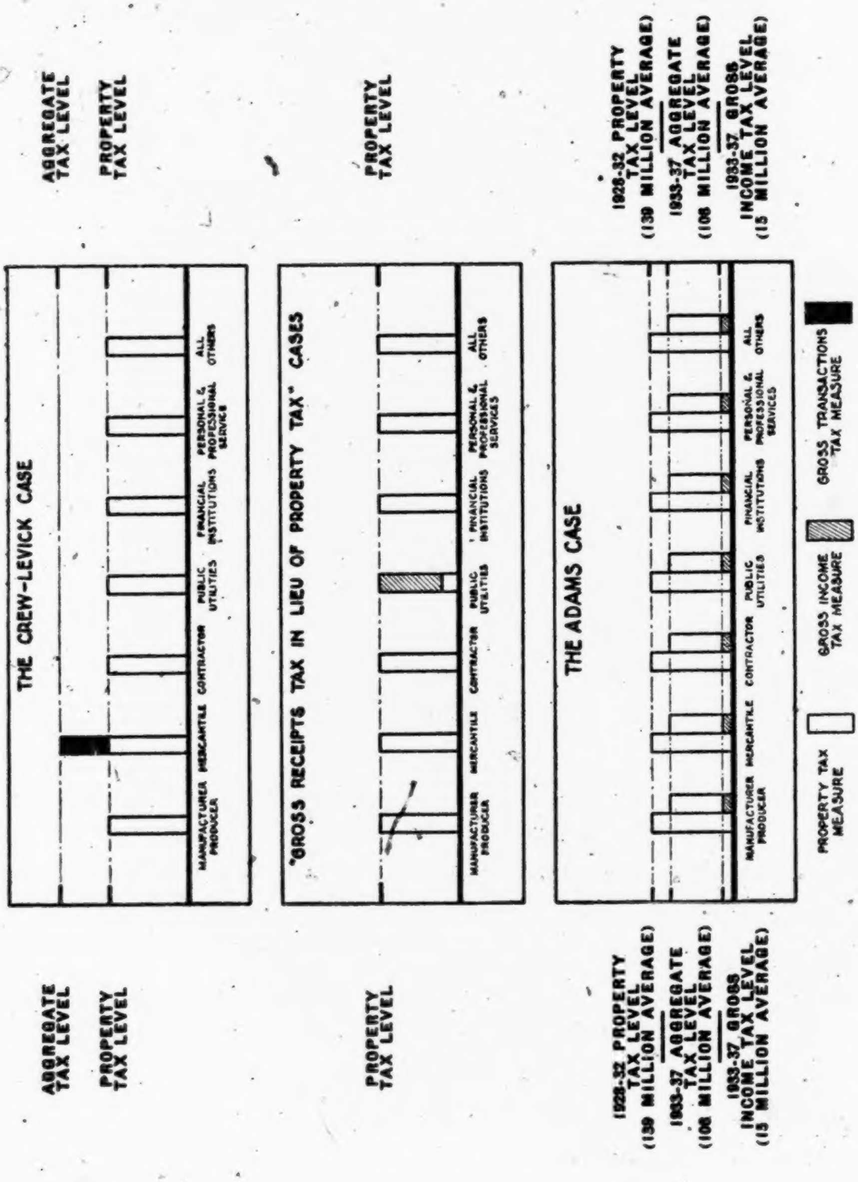
Acts of Indiana, 1933, page 1085.

APPENDIX "D"

This graph is merely illustrative of certain phases of Appellee's argument.



APPENDIX "E"

TOTAL TAXES COLLECTED

BY

THE STATE, COUNTIES, TOWNSHIPS, CITIES, TOWNS AND SCHOOL CORPORATIONS OF THE STATE OF INDIANA

	Fiscal Year 1928-1929 Ending 9/30	*Fiscal Year 1929-1930 Ending 9/30*	*Fiscal Year 1930-1931 Ending 9/30*	*Fiscal Year 1931-1932 Ending 9/30*	*Sept. 30, 1932 June 30, 1933 (9 months)**	*Fiscal Year 1933-1934 Ending 6/30*	*Fiscal Year 1934-1935 Ending 6/30*	*Fiscal Year 1935-1936 Ending 6/30*	*Fiscal Year 1936-1937 Ending 6/30*	*TOTAL*
Taxes on Property	$136,451,643.17	$144,149,820.78	$143,438,784.71	$135,421,445.18	$112,386,878.08	$ 87,437,220.88	$ 95,575,961.18	$ 93,145,960.32	$ 99,688,926.18	$1,047,696,640.48
Poll Taxes	1,394,173.07	1,328,976.96	1,275,224.62	1,435,463.46	1,257,822.01	1,412,527.60	1,487,443.14	1,572,426.55	1,636,256.51	12,800,313.92
Insurance Taxes	1,991,437.81	2,089,566.90	1,843,382.49	1,738,769.24	773,881.43	1,467,895.59	1,703,149.78	1,895,373.26	1,913,812.34	15,417,268.84
Transportation Taxes	94,885.25	83,464.90	83,211.40	75,224.21	67,938.60	62,027.64	62,992.44	59,045.72	59,000.50	647,790.66
Vessel Tonnage Taxes	1,349.63	1,209.87	1,112.58	1,231.80	711.51	3,498.83	2,348.75	2,039.97	3,126.76	16,629.70
Dog Taxes	408,024.12	423,340.90	422,971.59	415,164.12	357,037.03	346,558.94	378,515.81	397,441.61	304,719.23	3,453,773.35
Inheritance Taxes	1,213,049.59	1,450,554.80	1,943,491.59	2,090,229.95	687,710.75	788,159.26	1,190,087.15	1,081,308.86	1,239,027.27	11,683,619.22
Gasoline Taxes	14,033,741.01	16,832,447.88	17,828,025.59	17,166,160.27	11,405,452.90	16,841,584.73	17,790,821.41	19,760,704.90	22,131,786.17	153,790,724.86
Excise Taxes					1,032,372.98	2,673,963.18	2,238,815.75	3,501,878.39	4,491,547.19	13,938,577.49
Intangibles					633,889.67	1,284,360.66	1,085,571.21	1,326,704.97	1,507,312.42	5,837,838.93
Motor Vehicle Weight Tax						40,620.65	29,164.81	667,899.79	510,528.01	1,248,213.26
Gross Income Tax						10,388,014.99	13,607,836.05	16,548,477.91	20,556,656.33	61,100,985.28
TOTAL	$155,588,303.65	$166,359,382.99	$166,836,204.57	$158,343,688.23	$128,603,694.96	$122,746,432.95	$135,152,707.48	$139,959,262.25	$154,042,698.91	$1,327,632,375.99

* State Fiscal year changed from October 1, to Sept. 30 to July 1, to June 30.